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FIDUCIARY INCOME TAX WORKSHOP

Office of Income Taxation Communications & Training Branch

IN200.Fiduciary Income Tax *October 2008*

CONTENTS

FIDUCIARY???

Just What Is a Fiduciary?

The term fiduciary applies to a person who occupies a position of special confidence toward another, who holds in trust property in which another person has the beneficial title or interest, or who receives and controls income of another (per 2008 U.S. Master Tax Guide).

What Exactly Does that Mean?

The person designated as the fiduciary may be an individual or corporation. For estates they are known as an executor or an administrator and for trusts they are known as trustees. For tax purposes, the fiduciary is responsible for filing any required Fiduciary Income Tax return. This correlates to an individual taxpayer being required to file an individual return if they meet the filing requirements or a corporation's responsibility to file any required corporate returns.

Kentucky Filing Requirements

- Every estate with gross income for the taxable year of $1,200 or over; and
- Every trust with gross income for the taxable year of $100 or over must file a fiduciary return.

Federal Filing Requirements

- Domestic estates with gross income for the tax year of $600 or more, or a beneficiary who is a nonresident alien; and
- Domestic trusts that have any taxable income for the tax year, gross income of $600 or more (regardless of taxable income), or a beneficiary who is a nonresident alien must file a fiduciary return.

INHERITANCE & ESTATE TAX FILING REQUIREMENTS

Inheritance Tax

The Kentucky inheritance tax is a tax on a beneficiary's right to receive property from a deceased person. There are three class categories of beneficiaries: Class A, Class B and Class C. Filing requirements are determined by the category applicable to the taxpayer.

Class A beneficiaries include:

Spouse, parent, child, grandchild, brother, sister, stepchild & stepgrandchild

If the date of death is after June 30, 1998, all Class A beneficiaries are exempt from paying Kentucky inheritance tax.

Class B beneficiaries include:

Niece, nephew, half-niece, half-nephew, daughter-in-law, son-in-law, aunt, uncle, who are related by blood, great grandchild. Great niece or great nephew are not Class B beneficiaries. Class B beneficiaries receive a $1000 exemption and the tax rate is 4% – 16%.

Class C beneficiaries include:

All persons not included in the Class A & Class B categories. Class C beneficiaries receive a $500 exemption and the tax rate is 6% - 16%.

> **Note:** An inheritance tax return must be filed by the fiduciary (personal representative) **only** when inheritance tax is owed or when a Federal Estate & Gift Tax Return (Form 706) is required to be filed or if any part of the estate is passing to taxable beneficiaries. In this situation, a return must be filed even if no tax is due.

Estate Tax

Kentucky does not currently collect estate tax. Per the provisions of The Economic Growth and Tax Reconciliation Act of 2001 the credit for state death taxes was reduced 25% per year, so as of 2005 the estate tax has been eliminated.

For additional information on Inheritance and Estate Tax issues, contact:

Financial Tax Section Kentucky Department of Revenue P.O. Box 181 Frankfort, Kentucky 40602 – 0181 502-564-4810

TRUST INFORMATION

DEFINITION OF TRUST/TYPES OF TRUSTS

A **trust**, as defined by the 2008 U.S. Master Tax Guide, paragraph 501, is:

> A separate taxable entity for federal income tax purposes. A "trust" usually involves an arrangement created by will upon the creator's death or by a trust instrument that may take effect during the creator's life. Under either arrangement, a trustee takes title to the property in order to protect or conserve it for the beneficiaries. Usually the beneficiaries of such a trust do no more than accept its benefits.

The essential elements of a trust are it's name, it's address, it's stated purpose, the name of the trustee or trustees, the powers of the trustee(s), the names of each beneficiary, the percentage of beneficial interest held by each beneficiary, name of a successor trustee in the event the present trustee is unable to serve, and the name(s) of successor beneficiaries in event of the death of the primary beneficiaries.

A trust is usually created as a tax benefit. The trust is a vehicle of avoiding a higher tax bracket or various taxes imposed such as estate and inheritance tax.

Types of trusts that are generally reported to Kentucky include, but are not limited to, the following:

1) **Simple Trust**---A trust that is required to distribute all of its income currently and has made no provision for charitable contributions. Capital gain income may be required to stay in the corpus* and will not be distributed, but this is still a simple trust. The "income" required to be distributed in order to qualify for classification, as a simple trust is the income under local law and the governing instrument (Trust instrument). Generally, this will include only ordinary income, because capital gains, under most trust instruments and state laws, are considered corpus. A trust will lose its classification as a simple trust for any year during which it distributes its corpus*. Thus, a trust can never be a simple trust during the year of termination or in a year of partial liquidation.

   ***corpus--** the asset(s) contributed to the trust; basis; principal

2) **Complex Trust**---All trusts other than those that do not qualify as a simple trust.

3) **Grantor Trust**---Grantor trusts are trusts in which some or all income produced is passed straight to the beneficiary or beneficiary's spouse and is taxed to the beneficiaries whether distributed or not. Generally, items of income, deduction, or credit that are treated as belonging to a trust grantor or another person are not reported by the trust on Kentucky Form 741. Instead, these items are reflected on the individual income tax return of the grantor (or other person who is taxable on the trust income). This information is required to be attached to the grantor's individual income tax return each year income is earned by the trust. This attachment should be attached each and every year the trust earns income.

If a portion of the income earned by the grantor trust is not treated as passed straight to the beneficiary, a separate statement identifying the income items and credits that are being reported on the beneficiary's income tax return should be attached to Form 741 stating the name, taxpayer identification number and address of the person to whom the income is taxable and setting forth the income deductions and credits. This information of the income treated as the trustee's is required to be attached to the grantor's individual income tax return each year income is earned by the trust.

4) **Charitable Remainder Trust**---A charitable remainder trust is a trust created so that distributions are specified amounts to be distributed to the beneficiaries with the remainder interest upon termination of the trust to be contributed to a specified charity. The distributions to the beneficiaries are based on a set amount or a percentage of the net fair market value of the trust's assets. Whenever there is a noncharitable income beneficiary, gifts of remainder interests in trust will qualify for a charitable contribution deduction only if the trust is a charitable remainder annuity trust or a charitable remainder unitrust.

5) **Pooled Income Fund** - A pooled income fund is a trust, operated by a charitable organization that enables you to retain a life income, claim a current income tax deduction, and make a future gift to charity. Because pooled income funds combine the contributions of all donors in a single investment fund, they are ideal for smaller contributions. **Note:** Form 5227, Split-Interest Trust Information Return must be filed for the pooled income fund.

6) **Pre-Need Funeral Trusts (Qualified Funeral Trusts**)--- A qualified pre-need funeral trust is an arrangement that would otherwise be treated as a grantor trust, under which an individual purchases funeral service or

merchandise for himself or for anther individual from a funeral home prior to death and funds the purchases via contributions to a trust. If the election is made, the income tax rate schedule generally applicable to estates and trusts is applied to the trust by treating each beneficiary's interest as a separate trust. However, the trust is not entitled to claim a trust tax credit when calculating the tax. The trustee's election must be made separately for each such "separate" trust. The trust pays the tax for the funeral trust beneficiaries on the fiduciary income tax return. This type of trust is relatively new.

7) **Small Business Tax Trust**---An electing small business trust (ESBT) is permitted to be a shareholder in an S Corporation, in tax years beginning after 1996. An electing small business trust is a trust that does not have any beneficiaries other than individuals, or estates eligible to be S corporation shareholders, except that charitable organizations may hold contingent remainder interest.

OTHER TRUSTS

Trusts can be used for a great variety of purposes in addition to those illustrated above. More than one of these categories may apply to a single trust.

TRUST INSTRUMENTS

The trust instrument is the governing document that sets forth the guidelines, beneficiaries, and assets involved in a trust. The trust instrument determines the type of trust, the length of the trust, what actions may be taken with the assets, who is responsible for paying the tax, and various other restrictions. The grantor or trustee sets up the trust instrument.

PARTIES OF A TRUST:

1. Grantor---Person(s) or entity that creates and provides assets for a trust entity.
2. Trustee---An individual or corporation in charge of duties associated with the trust.
3. Beneficiaries---Person/Entity designated to receive income or property from the trust.

KENTUCKY REQUIREMENT FOR A TRUST TO FILE

If a trust earns $100 or more in gross income, whether or not distributed, a Kentucky Fiduciary return must be filed. See KRS 141.190(c) for reference.

TRUST FILING PERIOD AND DUE DATE

The responsibility to timely file the fiduciary income tax return is the responsibility of the trustee. **A trust may only file on a calendar year basis**. Trusts may not choose to file with a fiscal year. The trust tax return is due on April 15th of the year following the tax year. The due date of the trust return is the same as for calendar year individual taxpayers. The Kentucky Form 40A102, Application for Extension of Time to File, may be used to request a six-month extension for filing. Also, the Kentucky Department of Revenue (KDOR) will accept a copy of the Federal automatic extension or a copy of the federally approved extended time to file.

WHO IS REQUIRED TO FILE THE TRUST RETURN

The trustee is responsible to file the return by the due date of the return.

TRUST TAX CREDIT

Kentucky allows a nonrefundable tax credit of $2.00 for each trust against the calculated tax liability for each tax year.

ESTATE INFORMATION

DEFINITION OF ESTATE/TYPES OF ESTATES

A **decedent's estate** is created upon the death of every individual. A decedent's estate is to report the taxable income earned after the date of death of an individual. Decedent's estates are considered separate taxable entities for Fiduciary Income tax purposes during the period of administration. The fiduciary (administrator, executor) is charged with collecting and conserving all of the deceased individual's assets and satisfying all liabilities. Also, the fiduciary is responsible for distributing the remaining assets to the heirs and/or beneficiaries.

TAXING INSTRUMENT OF DECEDENT'S ESTATE

In a **decedent's estate**, the decedent's will determines the distribution of income to the beneficiary(ies) and/or heirs. The will also determines who is responsible for paying the tax on the income, i.e. estate or beneficiary. If no will exists, the laws of the state determine how the income distribution is determined. (Reference Kentucky Statutes in Chapters 140 and 391.)

PARTIES OF A DECEDENT'S ESTATE:

1. Decedent---The deceased person who had assets at the time of death.
2. Executor or Administrator---An individual or corporation who is to administer the estate. The "executor" is appointed by the will; the courts assign the "administrator".
3. Beneficiary---Person(s) or entity(ies) designated to receive income or property from the estate.

A **Bankruptcy Estate** is a separate entity for a living individual who has filed Chapter 7 (liquidation) or Chapter 11 (business reorganization) of Title 11 of the U.S. Code. The individual who has entered into bankruptcy has assets that are controlled under the bankruptcy estate by authority of a court assigned and/or approved trustee. Any income earned from the assets in the bankruptcy status is reported as fiduciary income tax. The income and deductions are actually reported and tax calculated on the individual income tax return and the tax amount is then reported on the Fiduciary income tax return. A complete copy of the individual income tax return reporting the income and deductions must be attached to the Form 741.

PARTIES OF A BANKRUPTCY ESTATE:

1. Debtor---The person who has filed a petition for relief under the bankruptcy laws.
2. Trustee---A person appointed in a bankruptcy case to represent the interests of the bankruptcy estate and the unsecured creditors. The trustee's responsibilities include reviewing the debtor's petition and schedules, liquidating the property of the estate, and making distributions to creditors. The trustee may also bring actions against creditors or the debtor to recover property of the bankruptcy estate.
3. Creditor---A person to whom or business to which the debtor owes money or that claims to be owed money by the debtor.

TAXING INSTRUMENT OF A BANKRUPTCY ESTATE

A petition of intention is filed with the bankruptcy court. This petition will include the debts and debtors and the assets assigned to the bankruptcy. A judge of the bankruptcy courts must approve this petition while the assigned trustee administers the estate.

KENTUCKY REQUIREMENT FOR AN ESTATE TO FILE

If an estate earns $1200 or more in gross income, whether or not distributed, a Kentucky Fiduciary return must be filed. See KRS 141.190(b) for reference. Income that is reported on the initial Form 741 begins with Kentucky taxable income earned from the date of death. The **corpus** of a decedent's estate is not included in the taxable income. The corpus is the assets the taxpayer owned or earned prior to death. Only the income received by the estate from the decedent's date of death until the close of the estate is reported on the fiduciary income tax return.

ESTATE TAX FILING PERIOD AND DUE DATE

The administrator/executor is responsible for completing and filing the fiduciary income tax return by the due date, including extension, of the return. The administrator/executor may choose to file the tax return as either a calendar year or a fiscal year. Whichever election is made with the federal return must be used on the Kentucky return.

The beginning date on the initial return is the date of death. The fiduciary may choose to end the first year as of December of that year or he/she may choose a fiscal year that begins with that date of death and can run up to twelve months, but not to exceed a twelve-month period.

The calendar-year estate return is due on April 15th of the year following the tax year. (The due date is the same as individual calendar-year taxpayers). Fiscal year fiduciary tax returns are due three months and fifteen days after the close of the fiscal year. The Kentucky Extension of Time to File or the federal automatic extension allows the estate to file with an extended due date.

A final year fiduciary return for an estate is due three months and fifteen days from the termination of the estate.

WHO IS REQUIRED TO FILE THE ESTATE TAX RETURN

The executor or administrator of the estate is responsible to file the return by the due date of the return.

ESTATE TAX CREDIT

Kentucky allows a nonrefundable tax credit of $20.00 for each estate against the calculated tax liability per tax year.

NONRESIDENT TRUSTS AND ESTATES

Any trust or estate that is not a “resident” estate or trust is required to file a Kentucky Form 741 if income is received from Kentucky sources. All Kentucky laws and regulations that pertain to individual income tax also apply to nonresident trusts or estates. Kentucky does not tax items of intangible income to nonresidents.

An estate is considered a Kentucky resident estate if the decedent was a resident of Kentucky at the date of death. If the decedent was not a resident of Kentucky at the date of death, the only income that would need to be reported to Kentucky on the Form 741 would be income attributable to business income or real property.

Deductions claimed against the Kentucky income subject to tax are only allowed at the percentage the Kentucky income is to total income earned. The percentage of allowable deductions must be computed in the same manner as computing the allowable deduction for the Kentucky estates or trusts that have lesser income than the income of the overall estate or trust.

A trust is considered to be a Kentucky trust if the principal place of administration of the trust takes place in Kentucky. The principal place of administration of a trust is the trustee’s usual place of business where the records of the trust are kept, or at the trustee’s residence is he has no such place of business. This is based on Kentucky Revised Statute 386.655.

Nonresident trusts are not required to file Kentucky Form 741 unless income is received from Kentucky sources.

NONTAXABLE INCOME ATTRIBUTABLE TO NONRESIDENT BENEFICIARIES

Nonresident estates and trusts are not taxed on intangible income received from Kentucky sources, based on the laws also applicable to individual income tax.

103 KAR 19:010(6) states:

> Nonresident Estate or Trust and Nonresident Beneficiaries. A nonresident estate, trust, or beneficiary is subject to tax only on income received from real or tangible personal property located in Kentucky.

Income reported as a distribution on the Kentucky Schedule K-1, Form 741 to a nonresident beneficiary of Kentucky is subject to individual income tax with the exception as provided in this regulation listed.

FIDUCIARY INCOME TAX LAWS

As provided by the following statute and administrative regulation, Kentucky fiduciary income tax laws are based on individual income tax laws. The few exceptions that exist are those allowed by specific federal laws dealing with certain allowable deductions on the fiduciary return.

Kentucky Revised Statute 141.190(2) in part, states:

> Any fiduciary required to make a return under this chapter shall be subject to **all** the provisions of this chapter that apply to individuals.

Additionally, 103 KAR 19.010 in part, states:

> **All** provisions of KRS Chapter 141 (and related administrative regulations) that apply to individuals shall also apply to fiduciaries and returns filed by fiduciaries, except when such provisions conflict with provisions dealing specifically with fiduciaries.
>
> Taxable income of an estate or trust is net income as defined in KRS 141.010(11) **except:**
>
> - The standard deduction permitted individuals in KRS 141.080 is not allowed;
> - Federal estate tax paid on income accrued at the date of death of a decedent is deductible;
> - Deductions that have been allowed on the Kentucky inheritance tax return or the Kentucky individual income tax return cannot be claimed on the fiduciary income tax return; and
> - Any deductions (or federal tax) related to nontaxable income are not allowed

TRADITIONAL KENTUCKY TO FEDERAL INCOME DIFFERENCES

Kentucky individual and corporation income tax laws are based on the Internal Revenue Code reference date of December 31, 2006 per KRS 141.010(3). Thus, the federal and Kentucky fiduciary income reported as subject to tax is identical with the exceptions of the Kentucky traditional differences that are allowed to individual taxpayers. These traditional differences include:

- Interest from federal obligations
- Retirement income from local, state, and federal government plans
- Benefits from the U.S. Railroad Retirement board
- Capital gains on Kentucky Turnpike Bonds
- National Tobacco Settlement income
- Other State's Municipal Government Bond Interest
- Capital Gain on property taken by Eminent Domain

DIFFERENCES IN ALLOWABLE FIDUCIARY INCOME TAX DEDUCTIONS AND INDIVIDUAL INCOME TAX DEDUCTIONS

Deductions to income that are allowed for individual income tax are the same for the fiduciary income tax with two differences.

The first difference is that the charitable deductions are not limited to the amount of adjusted gross income reported on the fiduciary income tax return, as individual taxpayers are required to do. The Form 741 includes a Schedule A to compute the allowable charitable contribution. (Schedule A will be introduced later in the material.)

The second difference in deductions for the fiduciary income tax return is an allowance for administrative/fiduciary fees paid by the estate. An attorney or accountant fee is allowed on the individual income tax return if it is related to the collection or protection of taxable income. More specifics on the administrative/fiduciary fee will be discussed in detail later in the material.

INCOME AND DEDUCTION ITEMS REPORTED ON THE KENTUCKY FORM 741

As stated previously, Kentucky individual income tax and fiduciary income tax are based on federal tax laws. Therefore, the income reported on the Kentucky fiduciary income tax return starts with the federal adjusted total income from federal Form 1041, Line 17.

INCOME ITEMS TO BE REPORTED

All items of income subject to taxation for individual income tax are also subject to tax for fiduciary income tax. These items include:

Wages, salaries, and tips
Interest and Dividend income
Alimony received
Business Income from Sole Proprietorship Business
Capital Gains and/or Losses
Individual Retirement Arrangement (IRA) Distributions
Pensions and Annuities
Rental Real Estate Income
Royalties
Pass-through income from Partnerships, S Corporations, trusts and/or estates
Farm income from farm activity or farm rentals
Unemployment Compensation
Prizes and Awards
Gambling Winnings including lottery winnings
Jury Duty Fees
Other Miscellaneous income items

Items of income reported on the federal Form 1041 begin with interest income earned in the taxable year by the estate or trust. This interest income is reported on Line 1. Likewise, the dividend income earned by the estate or trust is reported on Line 2 of the Form 1041. Lines 3 through 8 lists other types of income, which are applicable to individual income taxpayers, that are required to be reported on the fiduciary income tax return.

Copies of all schedules applicable to the income reported on the federal Form 1041, such as the farm schedule and the supplemental income schedule, should be attached to the Kentucky Form 741, along with the Form 1041. The exception to this is Schedule D, Capital Gains and Losses. Different tax rates may apply to capital gain income for federal purposes. Kentucky taxes capital gain income as ordinary income.

Kentucky has retained the Fiduciary Schedule D, Form 741 to report the Kentucky gains and losses. Capital gain losses and loss carryover amounts normally remain in the estate or trust and are not distributed. In addition, Kentucky does have some traditional differences, such as depreciation, mentioned previously.

Differences in income are to be computed and entered on the Kentucky Fiduciary Income Tax return as an addition or subtraction. This will be discussed in depth later in the material.

ALLOWABLE DEDUCTIONS

Like income items, allowable deductions are based on the IRC. Therefore, the deductions claimed on federal Form 1041 are allowed on Kentucky Form 741. In general, an estate or trust is allowed deductions for those ordinary and necessary expenses incurred in carrying on a trade or business, those incurred in the production of income or the management or conservation of income-producing property, and those incurred in connection with the determination, collection, or refund of any tax.

Please be aware, however, that **the deductions must be attributable to income being taxed by Kentucky**, i.e., the deductions may need to be prorated based on any tax-exempt income.

The following are **allowable deductions**:

1. **Interest Paid**---The amount of interest paid or incurred by the estate or trust on amounts borrowed by the estate or trust, or on debt acquired by the estate or trust (i.e., outstanding obligations from the decedent) that is not claimed elsewhere on the return are an allowable deduction. Do not include interest paid on indebtedness incurred or continued to purchase or carry obligations on which the; interest is wholly exempt from income tax. Personal interest is not deductible. Examples of allowable interest deduction items include: Investment interest (subject to limitations); qualified resident interest; interest payable on unpaid portion of the estate tax attributable to the value of a reversionary or remainder interest in a property.

2. **Taxes---**Deductible taxes on the fiduciary return are the same as on the individual income tax return, i.e., local income tax or real property tax. Also, the generation-skipping transfer tax imposed on income distributions is an allowed deduction on the fiduciary return. **Do not include federal fiduciary tax paid on the Form 1041**; this is not an allowable deduction as federal tax paid is not an allowable deduction on the individual income tax return.

3. **Fiduciary Fees---**The fees paid to or incurred by the fiduciary for administering the estate or trust during the tax year is an allowable deduction.

4. **Charitable Deduction---**Amounts of gross income that are paid under the terms of the will or governing instrument for a charitable purpose* is allowed as a deduction. (*Charitable purpose as defined under IRC section 170(c).)

5. **Attorney, accountant, and return preparer fees**---Amounts paid to an attorney, accountant, or return preparer may be allowed as a deduction, as stated previously, for those ordinary and necessary expenses incurred in carrying on a trade or business, those incurred in the production of income or the management or conservation of income-producing property, and those incurred in connection with the determination, collection, or refund of tax.

6. **Other Deductions NOT limited to the 2% AGI Floor**---These are deductions that are not claimed elsewhere on the return. Examples of these deductions are:

   a. Bond premiums, which need to be amortized from taxable bonds, acquired before October 23, 1986.
   b. Casualty and Theft Losses incurred in the tax year. Form 4684 must be attached.
   c. Deductions for clean fuel vehicles.
   d. Net Operating Loss Deduction.

7. **Allowable Miscellaneous Itemized Deductions subject to the 2% AGI floor.** These deductions are the same miscellaneous deductions as allowed on the individual income tax return. These deductions also include expenses for the production or collection of income under section 212, such as investment advisory fees, subscriptions to investment advisory publications, and the cost of safe deposit boxes.

REMEMBER

Tax exempt income must be considered in computation of allowable deductions for Kentucky. If there are differences in adjusted gross income for Kentucky and federal purposes, then deductions must be prorated based on the percentage of Kentucky to Federal AGI. If the Kentucky adjusted gross income and federal adjusted gross income are the same, no adjustment is necessary.

COMPUTING THE ADJUSTED TOTAL INCOME OR LOSS

The total income reported on federal Form 1041, Line 9, minus any allowable deductions generates the federal Adjusted Total income or loss. This is the starting point for the Kentucky Fiduciary Income Tax Return and therefore that amount is entered on Line 1 of the Kentucky Form 741.

KENTUCKY FORM 741
FIDUCIARY INCOME TAX RETURN

The fiduciary income tax return is designed to report the income earned from an estate or trust. The fiduciary income tax is imposed on income earned by the estate after the date of death of an individual, before all assets are distributed and on income earned by a trust while the trust is in force.

The term **fiduciary** applies to a person who occupies a position of special confidence toward another, who holds in trust property in which another person has the beneficial title or interest, or who receives and controls income of another (per 2008 U.S. Master Tax Guide).

Estate: The assets a person leaves at the time of death may generate income. The income that is generated from these assets may be taxable. Also, income may be paid to the estate that was earned prior to the individual's death but not received until after the date of death may also be taxable. If the total of this income equals more than $1200, the Form 741 must be filed to report the income. The federal return equivalent to the Kentucky Fiduciary Income Tax Return, Form 741, is federal Form 1041.

Trust: A trust must report income earned from the assets owned by the trust if such income is $100 or more. The assets in a trust are "donated" by a grantor (an entity or persons who contribute assets such as capital and property). The income earned from these assets is to be reported on the fiduciary income tax return.

Examples of income earned by estates and trusts that should be reported on the fiduciary income tax return are:

- Interest income earned on savings accounts, certificates of deposits, and other interest bearing accounts.
- Sale of Capital Assets (rental real estate, business, farm, shares of stock, etc.)
- Annuity or payments received as a result of death
- Distributions from pass-through entities (S corps, partnerships, trusts, etc.)
- Rental Income
- Royalties
- Farm Income or Farm Rentals
- Wages, Salaries, and Tips (decedent earned prior to death but not received until after death)
- Miscellaneous Income (Example: Lottery Winnings, U.S. Tobacco Settlement Income)

FORM AND TAX YEAR INFORMATION

FORM NUMBER

The form number is located in the upper left-hand corner of the form. The tax year is located in the upper right-hand corner, similar to the individual income tax returns filed. Fiscal year filers are to enter the fiscal year dates in the center of the form, above the name and address area.

DEMOGRAPHIC INFORMATION

Demographic information is entered in the center, top portion of the return. The information to be included is as follows:

1. **NAME** of the estate or trust. (Example: John G. Smith Irrevocable Trust)
2. **NAME and TITLE** of the fiduciary. The fiduciary, in this case, is the person or persons handling the estate or trust. The fiduciary sometimes is a corporation or financial institution, such as Bank One or PNC Bank. The title of the fiduciary is generally administrator/-trix, executor/-trix, or trustee. (Example: Susie L. Smith, Trustee or Joseph Pulliam, Executor) Often times, a fiduciary can be titled as "co-", such as co-executor, co-administrator.
3. **ADDRESS** of the fiduciary. In this case, the fiduciary is, again, the person or persons administering the estate or trust. The address for the fiduciary is the address where all correspondence, refunds, tax notices from the Kentucky Department of Revenue are to be sent. Post Office box numbers with the town, city, and zip code are acceptable addresses.

IDENTIFICATION NUMBER

The Federal Identification Number (FEIN) is entered to the right of the estate's or trust's name. The federal government assigns the number. For many estates, a social security number will be used. The Department of Revenue does not currently assign identification numbers to estates or trusts.

An employee may search the KDOR"s current database by using the FEIN assigned to the trust or estate. The fiduciary tax information is stored on the individual income tax database. The individual income tax database is set up to include social security numbers that are congruent with the fiduciary's FEIN's. However, KDOR personnel do not always enter the FEIN when keying the fiduciary information.

DATE CREATED

Below the FEIN is an area to report the date the entity was created. This is the date the decedent died or the date the trust was established.

TELEPHONE NUMBER

To the right of the address information, you will see an area to include the telephone number of the fiduciary. This allows a KDOR employee to call the fiduciary if additional information is needed.

TYPE OF FIDUCIARY RETURN FILED

The type of return filed is indicated by the box(es) marked on the left side of the Form 741. The options are as follows:

1. **Simple Trust**---A number of different types of trusts exist and the simple trust is a trust that is required to distribute all of its income currently and has made no provision for charitable contributions.
2. **Complex Trust**--- All trusts other than those that do not qualify as a simple trust. Additional type trusts will be defined later in this material.
3. **Bankruptcy Estate**---This is separate entity for an individual who has filed Chapter 7 (liquidation) or Chapter 11 (business reorganization) of Title 11 of the U.S. Code.
4. **Pooled Income Fund**---A trust to which a person transfers an irrevocable remainder interest in property for the benefit of a public charity, while retaining an income interest in the property for the life of one or more beneficiaries living at the time of the transfer.
5. **Initial Return**---First return filed for the estate or trust.
6. **Amended Return**---A corrected filing of a return previously filed with the Cabinet.
7. **Final Return**---The last return to be filed by the entity, i.e., the estate or trust has been closed and/or finalized.

SIGNATURE ON RETURN AND TAX PREPARER INFORMATION

The fiduciary or an authorized representative must sign the Kentucky Form 741. If a corporation or bank is the acting fiduciary, the Federal Identification Number must be entered. If the fiduciary is an attorney or other individual functioning in a fiduciary capacity, they are to leave this space blank. They should not enter their individual social security number.

Anyone who is paid to prepare the tax return must sign the return and include their social security number or preparer tax identification number (PTIN), along with their complete address.

COMPLETING KENTUCKY FORM 741 – Line by Line

The Kentucky Fiduciary income tax return has undergone several major changes over the years. Prior to the 1999 tax year, the Kentucky fiduciary income tax return looked identical to the federal fiduciary income tax return in regards to the line entries for reporting income and deductions. For that reason, the Kentucky return was re-engineered to begin with the Federal Adjusted Total Income as reported on the federal form 1041 and allow adjustments to income on the Kentucky return. Further re-engineering of the fiduciary return resulted in adding a Schedule M to report Kentucky modifications to the Federal Adjusted Total Income.

LINE ONE---FEDERAL ADJUSTED TOTAL INCOME

The Federal Adjusted Total Income is the beginning point for Kentucky **Form 741, Line 1**. This amount is found on form 1041, Line 17.

LINE TWO---ADDITIONS TO FEDERAL ADJUSTED TOTAL INCOME

Enter on **Form 741, Line 2**, the amount from Schedule M, which is the income that is subject to tax by Kentucky but was not reported on federal Form 1041. The Kentucky Schedule M is on page two of Form 741; the specific line items of this schedule will be discussed later in this material.

LINE THREE---PORTION OF DEDUCTIONS ALLOCABLE TO ADDITIONAL KENTUCKY INCOME

Report on **Line 3, Form 741** any deductions allocated to the additional Kentucky income that is reported on Line 2. These deductions were not allowed on the federal form 1041, as the income reported on the Form 741, Line 2, is exempt for federal purposes. These additional deductions are subtracted from the additional income reported on Line 2.

LINE FOUR -- Mathematical Subtraction

Subtract **Line 3** (the additional deductions) from **Line 2** (the additional Kentucky income) to determine the correct amount that is to be added to the federal adjusted total income.

LINE FIVE-- Mathematical Addition

Add **Lines 1** (Federal Adjusted Total Income) to **Line 4** (the additional Kentucky Income).

LINE SIX – SUBTRACTIONS TO FEDERAL ADJUSTED TOTAL INCOME

Enter on **Form 741, Line 6**, amounts from Schedule M which is income that is exempt from tax by Kentucky but was not reported on federal form 1041.

LINE SEVEN -- PORTION OF DEDUCTIONS ALLOCABLE TO INCOME EXEMPT FROM KENTUCKY TAX

Form 741, Line 7 allows for the add-back of any deductions claimed on federal form 1041 that are attributable to Kentucky tax exempt income. As stated previously, only those deductions attributable to Kentucky and subject to tax are allowed. Therefore, the percentage of Kentucky income to total income must be calculated. To compute unallowable deductions, divide the Kentucky tax-exempt income by the total income of the fiduciary. Multiply total deductions by this percentage. Report the amount of unallowable deductions on Line 7.

LINE EIGHT --- Mathematical Subtraction

Subtract the unallowed deductions reported on **Line 7** from the Kentucky tax-exempt income reported on **Line 6**. Report this amount on **Form 741, Line 8.**

LINE NINE--- KENTUCKY ADJUSTED TOTAL INCOME OR (LOSS)

Adjusted Total Income or (Loss) – The instructions for **Line 9** direct us to subtract **Line 8** from **Line 5**. This results in the **Kentucky** adjusted total income.

LINE TEN---INCOME DISTRIBUTION DEDUCTION

If the estate or trust is required to distribute income currently or if it paid, credited, or was required to distribute any other amounts to beneficiaries during the tax year, the Schedule B must be completed.

> ******Not all estates or trusts are required to distribute the income. The trust or estate may elect to pay the tax. Then a distribution deduction is not calculated.***

Distributable Net Income (DNI) is an amount that sets the limit on the deduction for distributions to beneficiaries. It may also limit the amount of the distribution taxable to the beneficiary. The DNI of a domestic estate or trust generally consists of the same items of gross income and deductions that make up the taxable income of the estate or trust. The DNI may also include tax-exempt income, as these amounts would be distributed to the beneficiaries.

ALLOCATION OF DEDUCTIONS

All items of deductions that enter into the computation of DNI are allocated among the items of income reported in the following order:

1. All deductions directly attributable to a specific class of income are deductible from that income. For example, rental expenses are deducted from rental income.

2. Deductions that are not directly attributable to a specific class of income generally may be allocated to any class of income, as long as a reasonable portion is allocated to tax-exempt income. Examples of deductions not specific to a certain type of income include:
   - Fiduciary Fees
   - Safe deposit box rental fee
   - Personal property tax

3. Any excess deductions that are directly attributable to a class of income may be allocated to another class of income. However, in no case can excess deductions from passive activity be allocated to income from non-passive activities. Excess deductions to tax-exempt income cannot offset any other class of income.

   Except for the final year, you may not show any negative amounts for any class of income because the beneficiary may not claim losses or deductions.

   A net operating loss, a capital loss carryover, and deductions in excess of gross income for the year in which an estate or trust terminates can be deducted by a beneficiary succeeding to the property of the trust or estate. Excess deductions on termination of an estate or trust are allowed only in computing taxable income and must be taken into account in completing the beneficiary's tax preference items. Such deductions may not be used in computing the AGI. The deduction is claimed as an itemized deduction or capital loss on the beneficiary's tax return filed for the year in which the trust or estate terminates.

DOUBLE DEDUCTIONS PROHIBITED

Amounts deductible, as administration expenses or losses for inheritance (estate) purposes are not also deductible by the estate for income tax purposes. However, the estate can claim such items for income tax purposes if it files a statement (in duplicate) that the items have not been allowed as deductions for inheritance tax purposes and that all rights to deduct them for such purposes are waived. This prohibition against double deductions by estates extends to trusts and other persons for expenses or losses incurred.

LINE ELEVEN---PENSION INCOME EXCLUSION

Kentucky's pension income exclusion is available for the fiduciary if the fiduciary retains the income. Enter amount of pension income retained and attach Schedule P if more than $41,110.

> *Note: If pension income is distributed to the beneficiary(ies) then the pension income distributed will be reflected on the K-1's issued to the beneficiary(ies) on Line 5(a) of the K-1 and the pension income exclusion may be claimed by the beneficiary(ies) on the individual return.*

LINE TWELVE---FEDERAL ESTATE TAX DEDUCTION

If the estate or trust includes income in respect of a decedent (IRD) in its gross income, and the same amount was included in the decedent's gross estate for federal estate tax purposes, the estate or trust is allowed to deduct in the same tax year the income is included, that portion of the estate tax imposed on the decedent's estate that is attributable to the inclusion of the IRD in the decedent's estate.

Summarized: An item of income is being reported on federal Form 706, such as sale of stock. This same gain from the sale of stock is also reported on the Kentucky fiduciary return, Form 741. A deduction is allowed for the tax paid on federal Form 706 for the gain on this sale of stock because the gain is reported on both returns and tax is being paid twice.

Consequently, if the same income is being reported to Kentucky on Form 741 and is also reported on federal Form 706, Estate Tax Return, then a deduction for the tax paid on that same income on federal Form 706 can be calculated and claimed against income on Kentucky Form 741.

The amount of deduction is calculated similar to the amount of credit for tax paid another state on the individual income tax return. However, it is a **deduction** of income and **not** a **credit** against tax.

LINE THIRTEEN---Mathematical Addition

Add **Lines 10, 11** and **12.**

LINE FOURTEEN---Mathematical Subtraction

Determine total income of fiduciary by subtracting **Line 13** from **Line 9**.

LINE FIFTEEN---INTANGIBLE INCOME ATTRIBUTABLE TO NONRESIDENT BENEFICIARIES

Enter the amount of intangible income included in **Line 14** that is attributable to the nonresident beneficiaries and was not deducted on **Line 10** as an Income Distribution Deduction**.** A schedule that lists the nonresident beneficiary's name, address, social security number and amount of income or a copy of the nonresident beneficiary's federal Schedule K-1 should be attached to the Kentucky fiduciary return.

LINE SIXTEEN---Mathematical Subtraction

Determine taxable income of fiduciary by subtracting **Line 15** from **Line 14.**

LINE SEVENTEEN---TAX

Use the tax rate schedule, and if applicable, add additional tax calculated on Form 4972-K or Schedule RC-R to determine tax on amount on **Line 16**.

The Kentucky graduated tax rate is used to calculate the fiduciary income tax return. This graduated rate is the same as the tax rate schedule used for individual income tax.

Tax Rate Schedule:

If taxable income is:	*Tax before credit is:*
$ 0 - $3,000	2% of taxable income
$3,001 - $4,000	3% of taxable income minus $30
$4,001 - $5,000	4% of taxable income minus $70
$5,001 - $8,000	5% of taxable income minus $20
$8,001 -$75,000	5.8% of taxable income minus $84
$75,001 and up	6.0% of taxable income minus $334

LINE EIGHTEEN

Enter nonrefundable credits. Specify credit(s) claimed and attach supporting documentation.

Nonrefundable credits include the following:

- Corporation tax credit – worksheet required
- Limited liability entity tax credit – worksheet required
- Skills training investment tax credit
- Historic preservation restoration tax credit
- Credit for tax paid to another state – worksheet & copy of other state(s) return required
- Employer's unemployment tax credit – Schedule UTC required
- Recycling and/or composting tax credit – Schedule RC required
- Kentucky Investment Fund tax credit
- Coal incentive tax credit
- Qualified research facility tax credit
- Employer GED incentive tax credit
- Voluntary environmental remediation credit (Brownfield)
- Biodiesel credit
- Environment stewardship credit
- Clean coal incentive credit

LINE NINETEEN---TAX CREDIT

Enter $2 credit for trusts or $20 credit for estates.

LINE TWENTY---Mathematical Subtraction

Subtract **Lines 18** & **19** from **Line17(d)** to determine total tax. If negative number enter -0-.

LINE TWENTY ONE---Refundable Credits

Enter estimated payments on **Line 21(a)**; tax withheld on **Line 21(b)**; & if applicable, refundable corporation credit on **Line 21(c)**. Total and enter on **Line 21(d)**.

LINE TWENTY TWO---Mathematical Subtraction

Subtract **Line 21(d)** from **Line 20** to determine tax due, refund or amount to credit forward and mark check box accordingly.

SCHEDULE A---CHARITABLE DEDUCTION

If the fiduciary has made additions or subtractions to total income and claimed a charitable deduction on federal form 1041, Schedule A must be completed.

Estates and complex trusts are allowed an **unlimited** charitable deduction for amounts that are **paid** to recognized charities out of gross income during a tax year. The amounts paid must be set by the terms of the will or trust instrument.

An administrator or trustee may elect to treat amounts paid after the close of the tax year as having been paid in the earlier year for deduction purposes. This election must be made no later than the time, including extensions, prescribed by law for filing the income tax return for the tax year in which payments were made. This election to claim the amounts in the previous tax year cannot be revoked after the due date of that return.

For example, if a calendar year estate or trust makes a qualified charitable contribution February 10, 2008, from income earned in 2007 or prior, then the fiduciary can elect to treat the contribution as paid in 2007.

Estates, and certain trusts, may also claim an unlimited deduction for amounts of gross income permanently set aside for charitable purposes. This income set aside must be used for a specified purpose or it must be exclusively used for religious, charitable, scientific, literacy or educational purposes, or for the establishment, purchase or maintenance and operation of a nonprofit public cemetery.

The amount claimed as the charitable contribution deduction can be only claimed for amounts of contributions from **income**. Amounts paid to charities from the **corpus** are **not** deductible on the fiduciary income tax return. The corpus, as a reminder, is the basis of a fund or estate as distinct from income or interest.

The charitable deduction is computed on Form 1041, Schedule A. If the trust or estate has charitable deductions that are related to income not reported on the return, a separate schedule should be attached to the return.

Any adjustment to the allowable Kentucky deduction due to a difference in the amount of taxable income reported to Kentucky is reported on the Kentucky Schedule A of Form 741.

SCHEDULE B---INCOME DISTRIBUTION DEDUCTION

Schedule B must be completed to determine the income distribution deduction.

Line 1

The amount from Form 741, page 1, Line 9 is to be entered on Line 1, Schedule B. This is the Kentucky adjusted total income.

Line 2

Enter the adjusted tax-exempt interest. The tax-exempt interest is not taxable on the Kentucky Form 741 but it may be required to be distributed. Therefore to derive the true Income Distribution, we must include tax-exempt income into the equation.

Line 3

Enter all capital gains, whether or not distributed, that are reported on Kentucky Schedule D (Form 741), line 17, column 1. This is the amount of gains to the beneficiaries. If the Schedule D (Form 741) results in a net loss, enter zero.

Line 4

Enter amounts that are reported on federal Form 1041, Schedule B, line 4. These are the capital gains paid or permanently set aside for charitable purposes.

Line 5

Enter net capital gains included in the Kentucky Form 741, Schedule B, lines 1 or 2.

Line 6

Enter Kentucky gain from page one of Form 741 as a negative figure. This amount actually flows from the federal total adjusted income that is reported on Form 741, Line 1, plus any additions or subtractions of capital gains as reported on Lines 3 or 7 of Form 741.

Line 7

Add Lines 1 through 6 of the Kentucky Form 741, Schedule A. This creates the Distributable Net Income (DNI).

Line 8

Complex Trust Only - Enter the income for the tax year as determined under the trust instrument or local law.

Line 9

To be completed by simple trusts, complex trusts, and decedent's estates
Report the income that is required to be distributed currently, whether it is distributed or not. The determination of whether trust income is required to be distributed currently depends on the terms of the governing instrument and the applicable local law.

Line 10

Other amounts paid, credited or otherwise required to be distributed. This line is to be completed **only** by decedent's estates or a complex trust. These distributions consist of any other amounts paid, credited, or required to be distributed and are referred to as second tier distributions. Such amounts include annuities to the extent not paid out of income, mandatory and discretionary distributions of corpus, and distributions of property in kind.

Line 11

Total distributions. Add Lines 9 and 10 to arrive at the total distribution. If this amount is greater than Line 8, the amount should be reported as accumulated distributions on Schedule J (Form 1041).

Line 12

In figuring the income distribution deduction, the estate or trust is not allowed a deduction for any item of the DNI that is not included in the gross income of the estate or trust. Therefore, the DNI must be computed without the tax-exempt income. Enter on Line 12, the income reported as tax-exempt income.

Line 13

Tentative Income Distribution Deduction - Subtract Line 12 from Line 11.

Line 14

Tentative Income Distribution Deduction – Subtract Line 2 from Line 7.

Line 15

Compare Lines 13 and 14. Enter the smaller of Lines 13 and 14. This is your Income Distributable Deduction.

******REMINDER: Not all trusts and estates will have income distributions. Some estates and trusts are arranged so that the estate or trust pays the tax on the fiduciary return. The governing instrument defines if the estates and trusts are required to pay the tax or if the income items will be required to be reported to the beneficiaries and the return will claim an income distribution deduction.***

SCHEDULE M---MODIFICATIONS TO INCOME

The Form 741, Schedule M, was added to the fiduciary return to allow the taxpayer to adjust for any differences in Kentucky to federal income. If the trust or estate has no income differences it is not necessary to complete Schedule M.

Part I, Schedule M—Additions

This section is included so that the fiduciary can report those items of income that are subject to tax by Kentucky but exempt for federal tax purposes.

Line 1

Enter the interest received from bonds issued by other states. This bond interest is not taxable on the federal return but Kentucky does not exempt interest received from bonds issued by other states and therefore, this income must be reported on the Kentucky return,

Line 2

Enter any additional income received from partnerships, other fiduciaries, or S Corporations that is exempt for federal tax purposes but is subject to tax by Kentucky. This information is reported to the fiduciary by the Schedules K-1 received from any S corporations or partnerships in which the trust or estate is involved or any fiduciary in which the trust or estate is a beneficiary.

Line 3

Enter on Line 3 other additions that are taxable to Kentucky and not included in federal adjusted total income. Examples include:

a. additions from partnerships and/or S corporations, estates, or trusts;
b. the portion of a lump-sum distribution reported on the federal return on which the 20 percent capital gains rate for federal income tax purposes was claimed;
c. the federal net operating loss deduction;
d. the passive activity loss adjustment;
e. difference in pension (3-year recovery rule that began in 1986 and was allowed through the1989 tax year. This recovery rule allowed employee contributions to a pension plan to be recouped in the first three years);
f. difference in gains or losses from the sale of intangible assets amortized under the provisions of the Revenue Reconciliation Act of 1993.

Line 4—Total Additions

Add Lines 1 through 3. This amount is the total additions to federal adjusted total income to move toward a true Kentucky adjusted total income. The amount calculated on Line 4 of Schedule M is reported on Form 741, page one, Line 2.

PART II, Schedule M—Subtractions

This section is included so that the fiduciary can report those items of income that are exempt from Kentucky tax but subject to tax for federal tax purposes.

Line 5

Interest from U.S. Government Obligations is not taxable to Kentucky based on Kentucky Statutes. Any interest income received from U.S. Government Obligations that has been reported on the federal Form 1041 should be reported on Schedule M, Line 5.

Line 6

Enter any income received from partnerships, other fiduciaries, or S Corporations that is exempt under Kentucky Statutes but reported on the federal Form 1041. This information is reported to the fiduciary by the Schedules K-1 received from any S corporations or partnerships in which the trust or estate is involved or any fiduciary in which the trust or estate is a beneficiary.

Line 7

Form 741, Schedule M, Line 7 allows for other subtractions from the federal adjusted gross total income not listed above. Other subtractions may include:

- Kentucky net operating loss deduction;
- Passive activity loss adjustment (see Form 8582-K and instructions;
- U.S. Tobacco Settlement Fund income
- Differences in the gains (losses) from the sale of intangible assets amortized under the provisions of the Revenue Reconciliation Act of 1983; etc.

Line 8-- Total Subtractions

Add Lines 5 through Line 7. This amount is the total subtractions to federal adjusted total income and is reported on Form 741, page one, Line 6.

SCHEDULE K-1

The Schedule K-1 is used to report the beneficiary's share of income, deductions, and a credit from a trust or a decedent's estate.

The fiduciary must file Schedule K-1 to report any income distribution deduction claimed. A copy of each beneficiary's Schedule K-1 is attached to the Form 741. The number of Schedules K-1 attached should be indicated on the front of the Form 741 below the name and address area.

The name of the estate or trust is entered on the top line (below the fiscal year information).

To the right, top portion you will see a place to include the estate's federal identification number along with the name of the fiduciary (person or agent) and the address of the fiduciary.

To the top left side you will note a place for the entry of the beneficiary's identification number which is an individual's social security number or an entity's FEIN. The name and address of the beneficiary should be included.

Next, you will see all income and deduction items listed on the left side of the Schedule K-1. These are the same items as listed on the fiduciary income tax return. All items of income reported on the fiduciary income tax return will retain their same character and will flow to the applicable lines on the Schedule K-1.

If more than one beneficiary exists, each Schedule K-1 will report each beneficiary's proportionate share, as per below example.

TOTAL INCOME (INTEREST) $10,000

	Share	Schedule K-1 should reflect
Beneficiary A	50%	$5,000
Beneficiary B	30%	$3,000
Beneficiary B	20%	$2,000

The beneficiary's income is considered to have the same proportion of each class of items entering into the computation of DNI that the total DNI of each class has to the DNI.

A distribution received from a fiscal year estate filer must be reported on the beneficiary's individual income tax return for the year in which the fiscal year ended.

CAPITAL GAIN OR LOSS

Capital gain is taxed to the estate or trust and the gain must be added to principal. However, when the gain is actually distributed to beneficiaries during the tax year, it is included in the computation of distributable net income and, therefore, is taxed to the beneficiary.

A net capital loss of an estate or trust will reduce the taxable income of the estate or trust, but no part of the loss is deductible by the beneficiaries. If the estate or trust distributes all of its income, the capital loss will not result in a tax benefit for the year of the loss. Losses from the sale or exchange of capital assets are generally excluded in computing distributable net income. However, they may be used to determine the net amount of capital gains that are paid, credited, or required to be distributed to any beneficiary during the tax year. On termination of an estate or trust, any unused capital loss carryover of the estate or trust is available to the beneficiaries.

KENTUCKY SCHEDULE D (FORM 741)

The capital gain and loss income generated by activity for an estate or trust is to be reported on the Capital Gains and Losses Schedule, Schedule D. Kentucky Schedule D for Form 741 has been created to report differences that may result in the amount of capital gains or losses earned due to the traditional tax differences in Kentucky and federal income taxation.

The Kentucky Schedule D allows the fiduciary or tax preparer to calculate the amount of gain that will be taxed on the fiduciary level and the amount taxed on the beneficiary level.

Short-term and long-term losses are to be reported separately according to how long the estate or trust held or owned the property. The holding period for short-term gains and losses is one year or less. Any gain or loss on property held over one year is long-term gain. However, property acquired by a decedent's estate from the decedent is considered as held for more than one year, i.e., long-term gain.

For noncash property distributions, a fiduciary may elect to have the estate or trust recognize gain or loss in the same manner as if the distributed property had been sold to the beneficiary at its Fair Market Value (FMV). This FMV is referred to as the "stepped-up value". The amount reported on the inheritance return is the FMV. This election applies to all distributions made by the estate or the trust during the tax year and, once made, may be revoked only with IRS consent.

The **capital loss limitation** for each tax year is $3000 for estates and trusts, the same as individuals. This loss may be carried from year to year within the estate or fiduciary indefinitely or until termination of the entity. Upon termination of the estate or trust, the loss is then available to flow to the beneficiaries as a distribution and is claimed on the beneficiary's return.

KDOR ADMINISTRATIVE PROCEDURES AND ISSUES

Fiduciary income tax has been assigned tax type “03”. Tax notices are issued with “03” entered as the tax type. The following information relates to the various mainframe applications relevant to fiduciary tax.

PF-3 Individual Income Tax Database

Fiduciary returns processed by KDOR may be found on PF3, the Individual Income Tax database. Information about fiduciary returns is shown as follows:

- Code “F” , indicating a fiduciary return will be reflected in Column T – type return
- Check number will not show under Check #
- Check number will show above Validating #
- Other columns same as Individual Income

Name Searches

It may be necessary to use the name search option on PF3 if unable to locate any information on the fiduciary when using the FEIN. The name search option should be searched with the estate’s or trust’s last name in the same order as searching for an individual’s taxpayer information. (Example: Theodore J. Lovings Trust U/A. This trust would be searched by entering: Lovings Theo or Lovings T J; Example: Jasper J. Jackson Estate: This estate would be searched by entering: Jackson Jasper Est or Jackson J J Est or Jackson Est)

PF-17 Tax Refund System

Refund overpayments for fiduciary income tax are created and approved on the Business Tax Refund System on PF17. On the first screen use Option C for Business Tax Refunds to create the refund. The approval process is the same as for Individual Income Tax returns.

PF-20 File Requisition

Requisitions to KDOR’s Central Files should include “03” as the tax type. Enter the appropriate FEIN or SSN to identify the trust or estate.

PF-22 Journal Vouchers

Journal vouchers (JV's) are often necessary to correct processing errors on fiduciary returns such as misapplied payments, name corrections, etc. Creating JV's for fiduciaries is similar to creating JV's for Individual Income Tax. Whenever money is being moved from one fiduciary to another fiduciary tax type "03" is used. For all other fiduciary JV's, including multiple JV's, use the same tax types as you would use for creating JV's for Individual Income Tax.

TRACKING FIDUCIARY CHECKS

It is sometimes necessary to track a missing fiduciary check. Most refund checks can be researched through e-Mars or by calling the Treasury Department. In the past, the check number required for tracking was the fiduciary check number minus the first two digits. The fiduciary check number is found in the left column on PF3. It is the first of two numbers listed in this column. The second number is the validating number of the return. Because procedures established by outside agencies are not in our control, be aware this procedure is subject to change.

ESTIMATED TAX PAYMENTS

Kentucky statute allows the DOR to impose an estimated tax penalty on fiduciaries if the estate or trust has not prepaid the required amount of tax during the taxable year. However, currently we do not impose this penalty on fiduciary returns.

If an estate or trusts elects to make estimated tax payments they should utilize Form 740-ES, the same form used by individual taxpayers, and enter their FEIN or Social Security number in the space individuals enter Social Security numbers.

BANKRUPTCY ESTATES

General correspondence concerning bankruptcy issues and fiduciary returns for bankruptcy estates is forwarded to the Department of Collections, Legal Support Branch for review in case any information is relevant to their cases. Returns that are filed with “0” due, balance due, or refund due are then sent to processing for their handling.

If the Trustee has attached a letter requesting a “Prompt Determination”, that request is forwarded to the Office of Field Operations, Audit Selection Section, to determine if additional review (specifically an audit) is needed. A “Prompt Determination” is a request from the Bankruptcy Trustee for a determination of any additional tax due on a specific tax account or return.

Revenue has 60 days to notify the trustee of our intentions to audit the returns or tax periods and we have 180 days to complete any audit. If a Prompt Determination is requested and we fail to respond within the required period, we could be barred from filing a Proof of Claim and forfeit any payments in that estate case.

Most of the time no further review is pursued. Occasionally, Corporation Income/License Tax Returns related to the Prompt Determination are assigned by the Audit Selection Section for audit.

Once the determination is made by the Audit Selection Section, the Legal Support Branch is notified and they contact the Trustee with the information – either return accepted as filed or further review required. The results of any audit/review are forwarded back to the Department of Collections, Legal Support Branch for notification to the Bankruptcy Trustee and filing of a Proof of Claim.

EXAMPLES

COMPREHENSIVE FIDUCIARY EXAMPLE FOR A TRUST

The amounts and computations in the following 1041 example are based on an assumed factual situation, designed to illustrate the preparation of a return for a complex testamentary trust.

For purposes of this return, it is assumed that Thomas Tyler, who died in 2000, created by his will a trust that provided that:

(**1**) An amount equal to two-thirds of the income is to be currently distributed to a niece, Mrs. Mary S. Warden, and a nephew, Mr. Harold Draper, in equal parts, for the duration of their respective lives.

(**2**) The balance of the annual income is to be accumulated and added to the corpus, which upon the death of both beneficiaries goes to designated remainder men. (None of the remainder men is a charitable organization.)

(**3**) The income is to be distributed as above after deduction for any expenses, including depreciation, of the trust. The trustee is required to otherwise keep the trust corpus intact.

<u>INCOME ITEMS</u>:

Interest income $5,000

Dividend income $2,000

Net Capital Gains $16,200

(Short term loss of $6,000 plus long term gain of $22,200)

Long Term Capital Gains.. ($22,200)

Net Rental Income..$25,471

($45,000 total rents - $2,000 depreciation expense & $17,529 other expenses including repairs, $950, heating costs, $10,000, insurance, $2,050, janitorial costs, $1,300 & real estate taxes, $3,220)

DEDUCTION ITEMS

Taxes..$1, 575

Fiduciary fees $675

Attorney, accountant, and return preparer fees $150

Exemption $100

Income Distribution Deduction......... determined by completing Schedule B

TAX & PAYMENT SECTION

Calculate total tax liability – complete Schedule G on page 2

Enter Trust's Estimated Tax Payments $7,000

Complete mathematical computations to determine if refund or tax due.

Additional Information Relevant to This Return

The income shown on page 1 of Form 1041 on Lines 1—8 and the deductions on Lines 10—15b are entered as if the entire net income were taxable to the trust. From the net income of the trust are deducted the amount distributed or required to be distributed to the beneficiaries (Line 18), certain estate or generation-skipping taxes (Line 19), and the appropriate exemption (Line 20). The remainder (Line 22) is the taxable income on which the fiduciary pays the tax.

Dividends in the Tyler Trust *are not* allocable to corpus. They are, therefore, apportioned between the trustee and beneficiaries. Each beneficiary's share is shown on Line 2 of a separate Schedule K-1.

Depreciation The trust instrument forming the basis of the example provides that the trust is to keep the corpus intact, thereby requiring it to maintain a reserve for depreciation. Accordingly, because the income set aside by the trustee for the depreciation reserve is equal to the allowable depreciation deduction, no depreciation is allocated to the beneficiaries on Line 5b of each Schedule K-1 of Form 1041.

Note If the $2,000 depreciation deduction for the Tyler Trust had been allocated equally among the beneficiaries and the trustee, under the terms of the trust or because of state law, the trust's depreciation deduction would amount to one-third of $2,000, or $667. In addition, each beneficiary's share of the depreciation ($667) would have appeared on Line 5b of the beneficiary's Schedule K-1.

Capital Gains The sale of stock that produced long-term capital gain took place on May 1, 2007. The governing trust instrument is silent on the treatment of gains from the sales of corpus. Under most state laws, such gains are not distributable to the life beneficiaries, but are added to, and become a part of, the corpus held for the remainder men unless the trust instrument directs otherwise. Accordingly, no part of this gain in the example is included on Schedule K-1 for the beneficiaries. It remains as capital gain income, taxable to the trust.

Deductions If an estate or trust has tax-exempt income, the deduction amounts claimed on Lines 10 through 15b must be reduced by an allocable portion attributable to tax-exempt income. This is done by multiplying the amount of each deduction by a percentage factor that is derived by dividing the total tax-exempt income by gross income (including tax-exempt income) included in distributable net income.

DISTRIBUTIONS DEDUCTION

The income distribution deduction is computed in different ways depending on whether distributions are less than or more than distributable net income (DNI). If the amount of such distributions is less than DNI, the amount of the actual distributions is used. If the amount of the distributions is more than DMI, the DMI must be computed by taking into account the miscellaneous itemized deductions after applying the 2% floor. An algebraic formula for this computation is provided in the Form 1041 instructions.

An estate or trust claims a deduction from income for distributions to beneficiaries, and the amount so allowed is included in the income of the beneficiaries (Code Sec. 661(a)). The distributions deduction claimed on Line 18, page 1, of Form 1041 is computed on Schedule B, Line 15.

Schedules K-1 must be attached for the beneficiaries of an estate or trust that claims the income distribution deduction. Also, the distribution deduction must be recomputed on a minimum tax basis on Schedule I. The deduction is the total of the amounts paid, credited or required to be distributed to the beneficiaries or the distributable net income, **whichever is less**. In either case, the amount must be adjusted to exclude any tax-exempt income (it is assumed that there is none in the example).

The amount of income required to be distributed currently in the example, $19,514, is **less** than the distributable net income of $29,271. Therefore, the income distribution deduction is $19,514. This amount is carried from Line 15, Schedule B, page 2, Form 1041, to Line 18, page 1.

DISTRIBUTABLE NET INCOME

Before the amount of the deduction for distributions to beneficiaries, to be entered on Line 18, page 1, of Form 1041 may be determined, it is necessary to compute distributable net income. DNI must also be determined before the separate Schedules K-1 for each beneficiary's share of income, deductions, and credits can be completed.

SCHEDULE B

The distributable net income, which is computed in Schedule B, page 2, of Form 1041, is the income of the trust for the current year that is available for distribution. It includes all tax-exempt interest and all dividends.

In the example, the amount of $45,471 entered on Line 1 of Schedule B is the trust's adjusted total income from Line 17, page 1, of Form 1041. This amount is computed by taking the trust's total income on Line 9 of page 1 and subtracting the trust's total deductions reported on Line 16 on page 1. Thus, the distributions deduction and the deduction for estate taxes attributable to income in respect of a decedent are disregarded. Adjustments for items of tax-exempt interest, etc., described above are to be accounted for on Lines 2 through 6 of Schedule B. In this example, since the capital gains are assumed not to be distributable to the beneficiaries, they are to be excluded from distributable net income and, accordingly, are deducted on Line 6 of Schedule B.

The deduction of $16,200 of capital gains leaves a distributable net income of $29,271, as noted on Line 7, Schedule B. This amount also is the trust's accounting (or Code Sec. 643(b)) income, which is determined under the terms of the governing instruments and the applicable local law, as reported on Line 8, Schedule B.

REQUIRED DISTRIBUTIONS & OTHER DISTRIBUTIONS

The amounts of income of the estate or trust required to be distributed currently to each beneficiary, whether distributed or not and any other amounts paid, credited, or required to be distributed during the tax year, are to be entered on Lines 9 and 10 of Schedule B, page 2, Form 1041. In the example, no amounts are entered on Line 10 because the only distribution made by the trust for 2007 was the required two-thirds of current income less expenses.

ON THE RETURN

The $19,514 in the example, which appears on Line 9 of Schedule B and constitutes the amount of income currently distributable to the beneficiaries, is computed from the income and deductions listed in the facts pertaining to this return:

Income:

Line 1: Interest on bank deposits, notes, and corporation bonds ....$ 5,000
Line 2: Dividends...$1,200
Line 5: Net rents...$25,471
Total **$31,671**

Deductions/Expenses:

Line 11: Taxes.. $1,575
Line 12: Fiduciary fees $675
Line 14: Return preparer fees $150
Total ....**$ 2,400**

Current income less expenses ($31, 671 - 2,400).....................................$29,271
Distributable to beneficiaries (2/3 of $29,271) $19,514

Since the trust instrument specifies that the beneficiaries are to share equally in two-thirds of the trust income after deduction of expenses, one-half of the $19,514, or $9,757, is assigned to Mary S. Warden, and $9,757 is assigned to Harold Draper.

SCHEDULE K-1

Schedule K-1 is used to report a beneficiary's share of the income, deductions, and credits from the estate or trust.

Each beneficiary must include in gross income the smaller of (1) the amounts paid, credited or required to be distributed, or (2) the proportionate share of distributable net income. Either is reduced by the share of distributable tax-exempt income (decreased by the share of expenses incurred in earning that income). The character of the income reported on each separate Schedule K-1 by the fiduciary should be the same as the items that enter into the computation of distributable net income.

If the total of the amounts paid, credited or required to be distributed is **more** than the amount of distributable net income shown in Schedule B, then the amounts that go into the computation of distributable net income are reported on each Schedule K-1 in proportion to each beneficiary's share of income.

If the total payments, credits, and required distributions are **less** than the distributable net income, only a proportionate part of each item entering into the computation of distributable net income is reported on Schedule K-1, according to the ratio of each particular item of income to the distributable net income. This is the situation in the case of the example as explained below.

If capital gains and losses are involved (see below) or a charitable deduction is claimed special computations are required to determine the beneficiaries' shares of income.

Capital Gains and Losses

Generally, capital gains are not included in distributable net income unless they are (1) allocated to income under the governing instrument or local law, (2) allocated to corpus and actually distributed to beneficiaries during the taxable year, (3) used, under the governing instrument or the practice followed by the fiduciary, in determining the amount which is distributed or required to be distributed, or (4) paid or to be used for charitable purposes so that a contributions deduction is allowed.

Capital losses are excluded from the computation of distributable net income. But if capital gains are distributed, any available capital losses are offset against the gains to determine the net capital gains distributed.

Completing Schedule K-1

In the example, there is no interest or other income exempt from tax, and no capital gains are distributable. This leaves only dividends and other taxable income to be reported on each separate Schedule K-1 (Form 1041).

Total income, exclusive of capital gains, includes dividends of $1,200, interest of 5,000, and net rental income of $25,471. Assuming they are not directly related to any income item, the following expenses are to be allocated in the fiduciary's discretion:

Personal property tax	$1,575
Trustee fees	$675
Fee for preparing income tax return	$150
Total	$2,400

ON THE RETURN

In this example, the fiduciary elects to reduce the rental income by these deductions. This leaves taxable dividends of $1,200, interest of $5,000, and rental income of $23,071 (net rents of $25,471 minus $2,400).

Because the total amount distributed, 19,514, is **less** than the distributable net income, $29,271, only proportionate parts of the dividends and the other taxable income are reported on each separate Schedule K-1.

The dividends allocable to the beneficiaries are determined by multiplying the gross dividends of $1,200 by a fraction with the actual amount distributed ($19,514) as the numerator and the distributable net income ($29,271) as the denominator. The result is $800 allocable to the beneficiaries, $400 to each.

Similarly, this fraction is applied to the interest and rental income to arrive at interest of $3,333 applicable to the beneficiaries, $1,667 to each, and rental income of $15,380, $7,690 to each.

On Schedule K-1 (Form 1041) for Mary S. Warden, interest of $1,667 is reported on Line 1 and qualified dividends of $400 are reported on Lines 2a and 2b. A similar Schedule K-1 would be prepared for Harold Draper.

Net short-term capital gains and net long-term capital gains are reported on Lines 3 and 4a—d, respectively, of Schedule K-1.

Rental income from real estate activities of $7,690 is reported on Line 7 of the example. The adjustment for minimum tax purposes are reported on Line 12, Schedule K-1, Form 1041, and also reported by each beneficiary on, Form 6251, Alternative Minimum Tax—Individuals.

The allocable portion of an estate tax deduction is reported on Line 10, Schedule K-1, Form 1041. Allocable portions of unused loss carryovers or excess deductions upon termination are reported on Lines l3a through l3d, and allocable portions of foreign taxes are reported on Line 11, Schedule K-1. A computation for each should be prepared on a separate sheet.

A number of miscellaneous items, not reported elsewhere on Schedule K-1, are reported on Line 14 or on an attached statement. These include the beneficiary's share of: (1) estimated taxes (9172); (2) tax-exempt interest (3) gross farming and fishing income; (4) investment income under Code Sec. i63(d); (5) foreign trading gross income as defined in Code Sec. 942(a); and (6) various tax credits.

SCHEDULE I

The Thomas Tyler Trust must complete all four parts of Schedule I, even though it has no alternative minimum tax liability, because it has made an income distribution to its beneficiaries in 2007. The John Tyler Trust is not subject to the tax because its regular tax of $4,846 exceeded its tentative alternative minimum tax (AMT) liability of $755.

The Thomas Tyler Trust has an adjusted total income of $45,471 (Line 17, Form iO4i) to which taxes of $1,575 (Line ii, Form 1041) are added to obtain an adjusted alternative minimum taxable income of $47,046 (Line 25, Schedule I) (the trust does not have any alternative minimum tax adjustments, tax preference items or net operating losses).

The trust is entitled to a distribution deduction on a minimum tax basis of $19,514 (Line 44, Schedule I), and the trust's allocable share of the alternative minimum taxable income (Line 29, Part I, Schedule I $27,532 ($47,046 - $19,514).

The portion of income for minimum tax purposes allocable to Mary S. Warden (reported on Line 7, Schedule K-1, Form 1041) is her share of the income distribution deduction computed on a minimum tax basis from Line 44 of Schedule I. The income distribution deduction computed on a minimum tax basis is allocated among the beneficiaries in the same manner as the income was allocated for regular tax purposes. Thus, one half of $19,514, or $9,757, is reported.

On her individual return, Mary S. Warden will report $1,667 in interest on Line 1, Part 1, Schedule B, and $400 in total dividends on Line 5, Part II, Schedule B, flowing to Form 1040. The $7,690 in rental income is reported on Part III, Schedule E, and flows to her Form 1040.

COMPUTATION OF TAX

The tax computation is made on Schedule G, page 2, Form 1041. The taxable income of the trust or estate on Line 22, page 1, Form 1041, is either multiplied by the rates appearing in the 2007 tax table or, if eligible, the trust or estate may use the applicable rate for net capital gains. The total tax liability (Line 7, Schedule C) is reported on Line 23, page 1, Form 1041.

The Thomas Tyler Trust has taxable income of $25,857, which is subject to the top marginal rate of 35%. Using the 2007 Tax Rate Schedule, the regular tax on that amount would be $8,156. However, the trust has net capital gains of $16,200 and may compute its tax liability using the appropriate capital gains tax rate (Part V, Schedule D, Form 1041). The maximum tax taking into account the capital gains tax rate, as shown on Line 35, Schedule D, is $4,846. Because this amount is smaller than the regular tax on Line 37, it is entered on Line 1a, Schedule C, Form 1041, and the box for Schedule D is checked.

COMPLETION OF RETURN

The declaration at the bottom of page 1 calls for the signature of the fiduciary, without a requirement of notarization. Financial institutions that act as trustees and submit estimated tax payments must provide their employee identification number (EIN). A person who received compensation for preparing the return must also sign. A completed federal form 1041 for the Thomas Tyler Trust follows.

Form **1041** Department of the Treasury—Internal Revenue Service

U.S. Income Tax Return for Estates and Trusts 2007

OMB No. 1545-0092

A Type of entity (see instr.):
- ☐ Decedent's estate
- ☐ Simple trust
- ☑ Complex trust
- ☐ Qualified disability trust
- ☐ ESBT (S portion only)
- ☐ Grantor type trust
- ☐ Bankruptcy estate–Ch. 7
- ☐ Bankruptcy estate–Ch. 11
- ☐ Pooled income fund

B Number of Schedules K-1 attached (see instructions) ▶

For calendar year 2007 or fiscal year beginning , 2007, and ending , 20

Name of estate or trust (If a grantor type trust, see page 14 of the instructions.): Thomas Tyler Trust

Name and title of fiduciary: Great Trust Co.

Number, street, and room or suite no. (If a P.O. box, see page 14 of the instructions.): 1000 Main St

City or town, state, and ZIP code: Frankfort KY 40601

C Employer identification number: 61 : 1324567

D Date entity created: 01/01/2000

E Nonexempt charitable and split-interest trusts, check applicable boxes (see page 15 of the instr.):
- ☐ Described in section 4947(a)(1)
- ☐ Not a private foundation
- ☐ Described in section 4947(a)(2)

F Check applicable boxes: ☐ Initial return ☐ Final return ☐ Amended return ☐ Change in trust's name ☐ Change in fiduciary ☐ Change in fiduciary's name ☐ Change in fiduciary's address

G Check here if the estate or filing trust made a section 645 election ▶ ☐

Income	1	Interest income	1	5,000
	2a	Total ordinary dividends	2a	1,200
	b	Qualified dividends allocable to: (1) Beneficiaries ________ (2) Estate or trust ________		
	3	Business income or (loss). Attach Schedule C or C-EZ (Form 1040)	3	
	4	Capital gain or (loss). Attach Schedule D (Form 1041)	4	16,200
	5	Rents, royalties, partnerships, other estates and trusts, etc. Attach Schedule E (Form 1040)	5	25,471
	6	Farm income or (loss). Attach Schedule F (Form 1040)	6	
	7	Ordinary gain or (loss). Attach Form 4797	7	
	8	Other income. List type and amount	8	
	9	**Total income.** Combine lines 1, 2a, and 3 through 8 ▶	9	47,871
Deductions	10	Interest. Check if Form 4952 is attached ▶ ☐	10	
	11	Taxes	11	1,575
	12	Fiduciary fees	12	675
	13	Charitable deduction (from Schedule A, line 7)	13	
	14	Attorney, accountant, and return preparer fees	14	150
	15a	Other deductions **not** subject to the 2% floor (attach schedule)	15a	
	b	Allowable miscellaneous itemized deductions subject to the 2% floor	15b	
	16	Add lines 10 through 15b ▶	16	2,400
	17	Adjusted total income or (loss). Subtract line 16 from line 9 — 17: 45,471		
	18	Income distribution deduction (from Schedule B, line 15). Attach Schedules K-1 (Form 1041)	18	19,514
	19	Estate tax deduction including certain generation-skipping taxes (attach computation)	19	
	20	Exemption	20	100
	21	Add lines 18 through 20 ▶	21	19,614
Tax and Payments	22	Taxable income. Subtract line 21 from line 17. If a loss, see page 23 of the instructions	22	25,857
	23	**Total tax** (from Schedule G, line 7)	23	4,846
	24	**Payments:** a 2007 estimated tax payments and amount applied from 2006 return	24a	7,000
	b	Estimated tax payments allocated to beneficiaries (from Form 1041-T)	24b	0
	c	Subtract line 24b from line 24a	24c	7,000
	d	Tax paid with Form 7004 (see page 23 of the instructions)	24d	
	e	Federal income tax withheld. If any is from Form(s) 1099, check ▶ ☐	24e	
		Other payments: f Form 2439 ________ ; g Form 4136 ________ ; Total ▶	24h	
	25	**Total payments.** Add lines 24c through 24e, and 24h ▶	25	7,000
	26	Estimated tax penalty (see page 24 of the instructions)	26	
	27	**Tax due.** If line 25 is smaller than the total of lines 23 and 26, enter amount owed	27	
	28	**Overpayment.** If line 25 is larger than the total of lines 23 and 26, enter amount overpaid	28	2,154
	29	Amount of line 28 to be: a Credited to 2008 estimated tax ▶ ; b Refunded ▶	29	2,154

Sign Here Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Signature of fiduciary or officer representing fiduciary | Date | EIN of fiduciary if a financial institution

May the IRS discuss this return with the preparer shown below (see instr.)? ☐ Yes ☐ No

Paid Preparer's Use Only
Preparer's signature | Date | Check if self-employed ☐ | Preparer's SSN or PTIN
Firm's name (or yours if self-employed), address, and ZIP code | EIN | Phone no. ( )

For Privacy Act and Paperwork Reduction Act Notice, see the separate instructions. Cat. No. 11370H Form **1041** (2007)

Schedule A **Charitable Deduction.** Do not complete for a simple trust or a pooled income fund.

1	Amounts paid or permanently set aside for charitable purposes from gross income (see page 24)	1	
2	Tax-exempt income allocable to charitable contributions (see page 24 of the instructions)	2	
3	Subtract line 2 from line 1	3	
4	Capital gains for the tax year allocated to corpus and paid or permanently set aside for charitable purposes	4	
5	Add lines 3 and 4	5	
6	Section 1202 exclusion allocable to capital gains paid or permanently set aside for charitable purposes (see page 25 of the instructions)	6	
7	**Charitable deduction.** Subtract line 6 from line 5. Enter here and on page 1, line 13	7	

Schedule B **Income Distribution Deduction**

1	Adjusted total income (see page 25 of the instructions)	1	45,471
2	Adjusted tax-exempt interest	2	
3	Total net gain from Schedule D (Form 1041), line 15, column (1) (see page 25 of the instructions)	3	
4	Enter amount from Schedule A, line 4 (minus any allocable section 1202 exclusion)	4	
5	Capital gains for the tax year included on Schedule A, line 1 (see page 25 of the instructions)	5	
6	Enter any gain from page 1, line 4, as a negative number. If page 1, line 4, is a loss, enter the loss as a positive number	6	(16,200)
7	**Distributable net income.** Combine lines 1 through 6. If zero or less, enter -0-	7	29,271
8	If a complex trust, enter accounting income for the tax year as determined under the governing instrument and applicable local law — 8		
9	Income required to be distributed currently	9	19,514
10	Other amounts paid, credited, or otherwise required to be distributed	10	
11	Total distributions. Add lines 9 and 10. If greater than line 8, see page 26 of the instructions	11	19,514
12	Enter the amount of tax-exempt income included on line 11	12	
13	Tentative income distribution deduction. Subtract line 12 from line 11	13	19,514
14	Tentative income distribution deduction. Subtract line 2 from line 7. If zero or less, enter -0-	14	29,271
15	**Income distribution deduction.** Enter the smaller of line 13 or line 14 here and on page 1, line 18	15	19,514

Schedule G **Tax Computation** (see page 27 of the instructions)

1	**Tax:** a Tax on taxable income (see page 27 of the instructions)	1a	4846		
	b Tax on lump-sum distributions. Attach Form 4972	1b			
	c Alternative minimum tax (from Schedule I, line 56)	1c			
	d **Total.** Add lines 1a through 1c ▶			1d	4846
2a	Foreign tax credit. Attach Form 1116	2a			
b	Other nonbusiness credits (attach schedule)	2b			
c	General business credit. Enter here and check which forms are attached: ☐ Form 3800 ☐ Forms (specify) ▶	2c			
d	Credit for prior year minimum tax. Attach Form 8801	2d			
3	**Total credits.** Add lines 2a through 2d ▶			3	
4	Subtract line 3 from line 1d. If zero or less, enter -0-.			4	4846
5	Recapture taxes. Check if from: ☐ Form 4255 ☐ Form 8611			5	
6	Household employment taxes. Attach Schedule H (Form 1040)			6	
7	**Total tax.** Add lines 4 through 6. Enter here and on page 1, line 23 ▶			7	4846

	Other Information	Yes	No
1	Did the estate or trust receive tax-exempt income? If "Yes," attach a computation of the allocation of expenses		✓
	Enter the amount of tax-exempt interest income and exempt-interest dividends ▶ $		
2	Did the estate or trust receive all or any part of the earnings (salary, wages, and other compensation) of any individual by reason of a contract assignment or similar arrangement?		✓
3	At any time during calendar year 2007, did the estate or trust have an interest in or a signature or other authority over a bank, securities, or other financial account in a foreign country?		✓
	See page 29 of the instructions for exceptions and filing requirements for Form TD F 90-22.1. If "Yes," enter the name of the foreign country ▶		
4	During the tax year, did the estate or trust receive a distribution from, or was it the grantor of, or transferor to, a foreign trust? If "Yes," the estate or trust may have to file Form 3520. See page 29 of the instructions		✓
5	Did the estate or trust receive, or pay, any qualified residence interest on seller-provided financing? If "Yes," see page 29 for required attachment		✓
6	If this is an estate or a complex trust making the section 663(b) election, check here (see page 29) ▶ ☐		
7	To make a section 643(e)(3) election, attach Schedule D (Form 1041), and check here (see page 29) ▶ ☐		
8	If the decedent's estate has been open for more than 2 years, attach an explanation for the delay in closing the estate, and check here ▶ ☐		
9	Are any present or future trust beneficiaries skip persons? See page 29 of the instructions		✓

Schedule I **Alternative Minimum Tax (AMT)** (see pages 29 through 37 of the instructions)

Part I—Estate's or Trust's Share of Alternative Minimum Taxable Income

1	Adjusted total income or (loss) (from page 1, line 17)	1	45,471
2	Interest	2	
3	Taxes	3	1,575
4	Miscellaneous itemized deductions (from page 1, line 15b)	4	
5	Refund of taxes	5	( )
6	Depletion (difference between regular tax and AMT)	6	
7	Net operating loss deduction. Enter as a positive amount	7	
8	Interest from specified private activity bonds exempt from the regular tax	8	
9	Qualified small business stock (see page 30 of the instructions)	9	
10	Exercise of incentive stock options (excess of AMT income over regular tax income)	10	
11	Other estates and trusts (amount from Schedule K-1 (Form 1041), box 12, code A)	11	
12	Electing large partnerships (amount from Schedule K-1 (Form 1065-B), box 6)	12	
13	Disposition of property (difference between AMT and regular tax gain or loss)	13	
14	Depreciation on assets placed in service after 1986 (difference between regular tax and AMT)	14	
15	Passive activities (difference between AMT and regular tax income or loss)	15	
16	Loss limitations (difference between AMT and regular tax income or loss)	16	
17	Circulation costs (difference between regular tax and AMT)	17	
18	Long-term contracts (difference between AMT and regular tax income)	18	
19	Mining costs (difference between regular tax and AMT)	19	
20	Research and experimental costs (difference between regular tax and AMT)	20	
21	Income from certain installment sales before January 1, 1987	21	( )
22	Intangible drilling costs preference	22	
23	Other adjustments, including income-based related adjustments	23	
24	Alternative tax net operating loss deduction (See the instructions for the limitation that applies.)	24	( )
25	Adjusted alternative minimum taxable income. Combine lines 1 through 24	25	47,046
	Note: *Complete Part II below before going to line 26.*		
26	Income distribution deduction from Part II, line 44 — 26: 19,514		
27	Estate tax deduction (from page 1, line 19) — 27:		
28	Add lines 26 and 27	28	19,514
29	Estate's or trust's share of alternative minimum taxable income. Subtract line 28 from line 25	29	27,532

If line 29 is:

- $22,500 or less, stop here and enter -0- on Schedule G, line 1c. The estate or trust is not liable for the alternative minimum tax.
- Over $22,500, but less than $165,000, go to line 45.
- $165,000 or more, enter the amount from line 29 on line 51 and go to line 52.

Part II—Income Distribution Deduction on a Minimum Tax Basis

30	Adjusted alternative minimum taxable income (see page 34 of the instructions)	30	47,046
31	Adjusted tax-exempt interest (other than amounts included on line 8)	31	
32	Total net gain from Schedule D (Form 1041), line 15, column (1). If a loss, enter -0-	32	
33	Capital gains for the tax year allocated to corpus and paid or permanently set aside for charitable purposes (from Schedule A, line 4)	33	
34	Capital gains paid or permanently set aside for charitable purposes from gross income (see page 34 of the instructions)	34	
35	Capital gains computed on a minimum tax basis included on line 25	35	(16,200)
36	Capital losses computed on a minimum tax basis included on line 25. Enter as a positive amount	36	
37	Distributable net alternative minimum taxable income (DNAMTI). Combine lines 30 through 36. If zero or less, enter -0-	37	30,846
38	Income required to be distributed currently (from Schedule B, line 9)	38	19,514
39	Other amounts paid, credited, or otherwise required to be distributed (from Schedule B, line 10)	39	
40	Total distributions. Add lines 38 and 39	40	19,514
41	Tax-exempt income included on line 40 (other than amounts included on line 8)	41	
42	Tentative income distribution deduction on a minimum tax basis. Subtract line 41 from line 40	42	19,514
43	Tentative income distribution deduction on a minimum tax basis. Subtract line 31 from line 37. If zero or less, enter -0-	43	30,846
44	**Income distribution deduction on a minimum tax basis.** Enter the smaller of line 42 or line 43. Enter here and on line 26	44	19,514

Part III—Alternative Minimum Tax

45	Exemption amount			45	$22,500 00
46	Enter the amount from line 29	46	27,532		
47	Phase-out of exemption amount	47	$75,000 00		
48	Subtract line 47 from line 46. If zero or less, enter -0-	48			
49	Multiply line 48 by 25% (.25)			49	0
50	Subtract line 49 from line 45. If zero or less, enter -0-			50	22,500
51	Subtract line 50 from line 46			51	5,032
52	Go to Part IV of Schedule I to figure line 52 if the estate or trust has qualified dividends or has a gain on lines 14a and 15 of column (2) of Schedule D (Form 1041) (as refigured for the AMT, if necessary). Otherwise, if line 51 is— • $175,000 or less, multiply line 51 by 26% (.26). • Over $175,000, multiply line 51 by 28% (.28) and subtract $3,500 from the result			52	755
53	Alternative minimum foreign tax credit (see page 35 of the instructions)			53	0
54	Tentative minimum tax. Subtract line 53 from line 52			54	755
55	Enter the tax from Schedule G, line 1a (minus any foreign tax credit from Schedule G, line 2a)			55	4,846
56	**Alternative minimum tax.** Subtract line 55 from line 54. If zero or less, enter -0-. Enter here and on Schedule G, line 1c			56	0

Part IV—Line 52 Computation Using Maximum Capital Gains Rates

Caution: *If you did not complete Part V of Schedule D (Form 1041), the Schedule D Tax Worksheet, or the Qualified Dividends Tax Worksheet, see page 36 of the instructions before completing this part.*

57	Enter the amount from line 51			57	5,032
58	Enter the amount from Schedule D (Form 1041), line 22, line 13 of the Schedule D Tax Worksheet, or line 4 of the Qualified Dividends Tax Worksheet, whichever applies (as refigured for the AMT, if necessary)	58	16,600		
59	Enter the amount from Schedule D (Form 1041), line 14b, column (2) (as refigured for the AMT, if necessary). If you did not complete Schedule D for the regular tax or the AMT, enter -0-	59	0		
60	If you did not complete a Schedule D Tax Worksheet for the regular tax or the AMT, enter the amount from line 58. Otherwise, add lines 58 and 59 and enter the **smaller** of that result or the amount from line 10 of the Schedule D Tax Worksheet (as refigured for the AMT, if necessary)	60	16,600		
61	Enter the **smaller** of line 57 or line 60			61	5.032
62	Subtract line 61 from line 57			62	0
63	If line 62 is $175,000 or less, multiply line 62 by 26% (.26). Otherwise, multiply line 62 by 28% (.28) and subtract $3,500 from the result ▶			63	0
64	Maximum amount subject to the 5% rate	64	$2,150 00		
65	Enter the amount from line 23 of Schedule D (Form 1041), line 14 of the Schedule D Tax Worksheet, or line 5 of the Qualified Dividends Tax Worksheet, whichever applies (as figured for the regular tax). If you did not complete Schedule D or either worksheet for the regular tax, enter -0-	65	9,257		
66	Subtract line 65 from line 64. If zero or less, enter -0-	66	0		
67	Enter the **smaller** of line 57 or line 58	67	5,032		
68	Enter the **smaller** of line 66 or line 67	68	0		
69	Multiply line 68 by 5% (.05) ▶			69	0
70	Subtract line 68 from line 67	70	5,032		
71	Multiply line 70 by 15% (.15) ▶			71	755
	If line 59 is zero or blank, skip lines 72 and 73 and go to line 74. Otherwise, go to line 72.				
72	Subtract line 67 from line 61	72			
73	Multiply line 72 by 25% (.25) ▶			73	
74	Add lines 63, 69, 71, and 73			74	755
75	If line 57 is $175,000 or less, multiply line 57 by 26% (.26). Otherwise, multiply line 57 by 28% (.28) and subtract $3,500 from the result			75	1,308
76	Enter the **smaller** of line 74 or line 75 here and on line 52			76	755

Form **1041** (2007)

SCHEDULE D (Form 1041) Department of the Treasury Internal Revenue Service	**Capital Gains and Losses** ▶ Attach to Form 1041, Form 5227, or Form 990-T. See the separate instructions for Form 1041 (also for Form 5227 or Form 990-T, if applicable).	OMB No. 1545-0092 2007

Name of estate or trust	Employer identification number

Note: *Form 5227 filers need to complete only Parts I and II.*

Part I **Short-Term Capital Gains and Losses—Assets Held One Year or Less**

(a) Description of property (Example: 100 shares 7% preferred of "Z" Co.)	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Sales price	(e) Cost or other basis (see page 40 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)
1a					
1 Co-Work Corp 7,000 shares common stock	2/6/2007	4/22/2007	44,000	50,000	(6,000_

b Enter the short-term gain or (loss), if any, from Schedule D-1, line 1b	1b	
2 Short-term capital gain or (loss) from Forms 4684, 6252, 6781, and 8824	2	
3 Net short-term gain or (loss) from partnerships, S corporations, and other estates or trusts	3	
4 Short-term capital loss carryover. Enter the amount, if any, from line 9 of the 2006 Capital Loss Carryover Worksheet	4	( )
5 **Net short-term gain or (loss).** Combine lines 1a through 4 in column (f). Enter here and on line 13, column (3) on the back ▶	5	(6,000)

Part II **Long-Term Capital Gains and Losses—Assets Held More Than One Year**

(a) Description of property (Example: 100 shares 7% preferred of "Z" Co.)	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Sales price	(e) Cost or other basis (see page 40 of the instructions)	(f) Gain or (loss) for the entire year Subtract (e) from (d)
6a					
6 Mixture Corp. 5,000 shares common stock	2/06/2002	5/1/2007	47.200	25,000	22.200

b Enter the long-term gain or (loss), if any, from Schedule D-1, line 6b	6b	
7 Long-term capital gain or (loss) from Forms 2439, 4684, 6252, 6781, and 8824	7	
8 Net long-term gain or (loss) from partnerships, S corporations, and other estates or trusts	8	
9 Capital gain distributions	9	
10 Gain from Form 4797, Part I	10	
11 Long-term capital loss carryover. Enter the amount, if any, from line 14 of the 2006 Capital Loss Carryover Worksheet	11	( )
12 **Net long-term gain or (loss).** Combine lines 6a through 11 in column (f). Enter here and on line 14a, column (3) on the back ▶	12	22.200

For Paperwork Reduction Act Notice, see the Instructions for Form 1041. Cat. No. 11376V **Schedule D (Form 1041) 2007**

Part III **Summary of Parts I and II**
Caution: *Read the instructions before completing this part.*

			(1) Beneficiaries' (see page 41)	(2) Estate's or trust's	(3) Total
13	**Net short-term gain or (loss)**	13		(6,000)	(6,000)
14	**Net long-term gain or (loss):**				
a	Total for year	14a		22,200	22,200
b	Unrecaptured section 1250 gain (see line 18 of the wrksht.)	14b			
c	28% rate gain	14c			
15	**Total net gain or (loss).** Combine lines 13 and 14a ▶	15		16,200	16,200

Note: *If line 15, column (3), is a net gain, enter the gain on Form 1041, line 4 (or Form 990-T, Part I, line 4a). If lines 14a and 15, column (2), are net gains, go to Part V, and* **do not** *complete Part IV. If line 15, column (3), is a net loss, complete Part IV and the* **Capital Loss Carryover Worksheet,** *as necessary.*

Part IV **Capital Loss Limitation**

16 Enter here and enter as a (loss) on Form 1041, line 4 (or Form 990-T, Part I, line 4c, if a trust), the **smaller** of:
a The loss on line 15, column (3) **or** **b** $3,000 . . . 16 ( )

Note: *If the loss on line 15, column (3), is more than $3,000,* **or** *if Form 1041, page 1, line 22 (or Form 990-T, line 34), is a loss, complete the* **Capital Loss Carryover Worksheet** *on page 42 of the instructions to figure your capital loss carryover.*

Part V **Tax Computation Using Maximum Capital Gains Rates**

Form 1041 filers. Complete this part **only** if both lines 14a and 15 in column (2) are gains, or an amount is entered in Part I or Part II and there is an entry on Form 1041, line 2b(2), and Form 1041, line 22, is more than zero.

Caution: *Skip this part and complete the worksheet on page 43 of the instructions if:*

- *Either line 14b, col. (2) or line 14c, col. (2) is more than zero, or*
- *Both Form 1041, line 2b(1), and Form 4952, line 4g are more than zero.*

Form 990-T trusts. Complete this part **only** if both lines 14a and 15 are gains, or qualified dividends are included in income in Part I of Form 990-T, and Form 990-T, line 34, is more than zero. Skip this part and complete the worksheet on page 43 of the instructions if either line 14b, col. (2) or line 14c, col. (2) is more than zero.

17	Enter taxable income from Form 1041, line 22 (or Form 990-T, line 34)			17	25,857		
18	Enter the **smaller** of line 14a or 15 in column (2) but not less than zero	18	16,200				
19	Enter the estate's or trust's qualified dividends from Form 1041, line 2b(2) (or enter the qualified dividends included in income in Part I of Form 990-T)	19	400				
20	Add lines 18 and 19	20	16.600				
21	If the estate or trust is filing Form 4952, enter the amount from line 4g; otherwise, enter -0- ▶	21					
22	Subtract line 21 from line 20. If zero or less, enter -0-			22	16,600		
23	Subtract line 22 from line 17. If zero or less, enter -0-			23	9,257		
24	Enter the **smaller** of the amount on line 17 or $2,150			24	2,150		
25	Is the amount on line 23 equal to or more than the amount on line 24? ☑ **Yes.** Skip lines 25 through 27; go to line 28 and check the "No" box. ☐ **No.** Enter the amount from line 23			25			
26	Subtract line 25 from line 24			26			
27	Multiply line 26 by 5% (.05)					27	
28	Are the amounts on lines 22 and 26 the same? ☐ **Yes.** Skip lines 28 thru 31; go to line 32. ☑ **No.** Enter the smaller of line 17 or line 22			28	16,600		
29	Enter the amount from line 26 (If line 26 is blank, enter -0-)			29	0		
30	Subtract line 29 from line 28			30	16,600		
31	Multiply line 30 by 15% (.15)					31	2,490
32	Figure the tax on the amount on line 23. Use the 2007 Tax Rate Schedule on page 27 of the instructions					32	2,356
33	Add lines 27, 31, and 32					33	4,846
34	Figure the tax on the amount on line 17. Use the 2007 Tax Rate Schedule on page 27 of the instructions					34	8,156
35	**Tax on all taxable income.** Enter the **smaller** of line 33 or line 34 here and on line 1a of Schedule G, Form 1041 (or line 36 of Form 990-T)					35	4,846

Schedule D (Form 1041) 2007

FLOW OF FORM 1041 FOR TYLER TRUST TO KENTUCKY FORM 741

The facts are the same for Kentucky except that only $1000 has been paid in for estimated tax.

To complete the Kentucky form 741, the following steps should be followed:

1) Start with the federal adjusted total income, as shown on federal form 1041, Line 17

2) Enter any additions and/or subtractions from Schedule M, Page 2 - if charitable deductions are claimed it may be necessary to complete Schedule A, Page 2,

3) Complete Schedule B, Page 2 to determine any income distribution

4) Complete Schedule P, Page 2 if necessary,

5) Complete mathematical calculations to arrive at Total Income,

6) If applicable, enter intangible income attributable to Nonresidents,

7) Compute tax using appropriate schedule(s),

8) Enter credits,

9) Calculate tax, refund or amount to credit forward, &

10) Complete additional information on page 2 and sign return.

The completed Kentucky Form 741 for the Thomas Tyler Trust follows.

Form 741
42A741
Department of Revenue
For calendar year or other taxable year beginning 01/01, 2007, and ending 12/31, 2008.

KENTUCKY FIDUCIARY INCOME TAX RETURN **2007**

Check applicable box:
- ☐ Decedent's estate
- ☐ Simple trust
- ☒ Complex trust
- ☐ Grantor trust
- ☐ Bankruptcy estate
- ☐ Pooled income fund
- ☐ ____________

Name of Estate or Trust: Thomas Tyler Trust
Federal Employer Identification Number: 61-1234567
Name and Title of Fiduciary: Great Trust Co.
Date Entity Created: 01/01/2000
Address of Fiduciary (Number and Street or P.O. Box): 1000 Main Street
Room or Suite Number:
City, State and ZIP Code: Frankfort Kentucky 40601
Telephone Number:

Check applicable boxes:
- ☐ Initial return
- ☐ Amended return
- ☐ Final return

Number of Schedules K-1 attached. ➤ __________ **(Copies Must Be Attached)**

➤ ***Attach a copy of the federal return including all schedules and statements.***

1. Federal adjusted total income (federal Form 1041, line 17)	1		45,471
2. Additions (from page 2, Schedule M, line 4)	2		
3. Enter the portion of deductions allocable to line 2	3		
4. Subtract line 3 from line 2	4		
5. Add lines 1 and 4	5		
6. Subtractions (from page 2, Schedule M, line 8)	6		
7. Enter the portion of deductions allocable to line 6	7		
8. Subtract line 7 from line 6	8		
9. Subtract line 8 from line 5. This is your Kentucky **adjusted total income (loss)**. Enter here and on page 2, Schedule B, line 1	9		45,471
10. Income distribution deduction (from page 2, Schedule B, line 15) **(attach Schedule(s) K-1)**	10	19,514	
11. Pension income exclusion (attach Schedule P, if more than $41,110)	11		
12. Federal estate tax deduction (attach computation)	12		
13. Add lines 10, 11 and 12	13		19,514
14. Total income of fiduciary (subtract line 13 from line 9)	14		25,857
INTANGIBLE INCOME ATTRIBUTABLE TO NONRESIDENTS INCLUDED IN LINE 14			
15. **Trusts or estates with income attributable to nonresident beneficiaries.** Enter the portion of intangible income included in line 14 that is attributable to **nonresident beneficiaries.** Enter zero if not applicable. See instructions	15		
16. Taxable income of fiduciary (subtract line 15 from line 14) **This is your taxable income**	16		
TAX COMPUTATION			
17. Tax: (a) tax rate schedule x (b) Form 4972-K ____ (c) Schedule RC-R ____ **Total**	17(d)		1,315
18. Nonrefundable credit(s) **(specify and attach supporting documents)**	18		
19. Enter **Tax Credit** *($2 for a trust; $20 for an estate). **This credit is not refundable***	19		2
20. **Total Tax** (subtract lines 18 and 19 from line 17d; if line 18 plus line 19 is more than line 17d, enter -0-)	20		1,313
21. (a) Estimated tax payments	21(a)	1,000	
(b) Withholding (attach wage and tax statements)	21(b)		
(c) Refundable Kentucky corporation tax credit (KRS 141.420(3)(c)) **(attach Kentucky Schedule(s) K-1 or Form(s) 725)**	21(c)		
(d) **Total** (add lines 21(a), (b) and (c))	21(d)		1,000
22. Subtract line 21(d) from line 20. Enter amount on ☒ tax due ☐ refund ☐ credit forward	22		313

I declare under the penalties of perjury that this return (including any accompanying schedules and statements) has been examined by me and, to the best of my knowledge and belief, is a true, correct and complete return.

Signature of Fiduciary or Agent | PTIN or Identification Number of Fiduciary or Agent | Date

Typed or Printed Name of Preparer Other Than Fiduciary or Agent | Identification Number of Preparer | Date

Refunds Mail to: **Kentucky Department of Revenue, Frankfort, KY 40618-0006.**
Payments Mail to: **Kentucky Department of Revenue, Frankfort, KY 40619-0008.**

➤ **Make check payable to: Kentucky State Treasurer.**

SCHEDULE A—CHARITABLE DEDUCTION (Do not complete for a simple trust or pooled income fund.)
Complete Schedule A only if you made additions to or subtractions from total income on page 1, lines 2 or 6 and claimed a charitable deduction on federal Form 1041.

1.	Kentucky taxable income that was paid or set aside for charitable purposes and was not reported on federal Form 1041, Schedule A, including additional capital gains. Enter here and include on Schedule M, line 7	1	
2.	Kentucky tax-exempt income that was paid or set aside for charitable purposes that was reported on federal Form 1041, Schedule A. Enter here and include on Schedule M, line 3	2	

SCHEDULE B—INCOME DISTRIBUTION DEDUCTION (See federal instructions.)

1.	Adjusted total income (enter amount from page 1, line 9)	1	45,471
2.	Adjusted tax-exempt interest	2	
3.	Net gain shown on Schedule D, Form 741, column 1, line 17 (if net loss, enter zero)	3	
4.	Enter amount included from federal Schedule A, line 4	4	
5.	Enter net capital gains included on Kentucky Schedule A, line 1 or line 2	5	
6.	Enter any Kentucky gains included on page 1, line 9 as a negative figure. If capital loss, enter as a positive figure. (Kentucky gain/loss includes federal figures plus Kentucky adjustments.)	6	(16,200)
7.	**Distributable net income** (combine lines 1 through 6)	7	29,271
8.	If complex trust, enter accounting income for tax years as determined under the governing instrument and applicable law	8	29,271
9.	Amount of income required to be distributed currently	9	19,514
10.	Other amounts paid, credited or otherwise required to be distributed	10	
11.	Total distributions (add lines 9 and 10) (If greater than line 8, see federal instructions.)	11	19,514
12.	Enter the amount of tax-exempt income included on line 11	12	
13.	Tentative income distribution deduction (subtract line 12 from line 11)	13	19,514
14.	Tentative income distribution deduction (subtract line 2 from line 7)	14	29,271
15.	**Income distribution deduction** (enter the smaller of line 13 or line 14 here and on page 1, line 10)	15	19,514

SCHEDULE M (FORM 741)

Part I—Additions to Federal Adjusted Total Income

1.	Enter interest from bonds issued by other states and their political subdivisions	1	
2.	Enter additions from partnerships, fiduciaries and S corporations (attach schedule)	2	
3.	Other additions (attach schedule)	3	
4.	Total additions. Enter here and on page 1, line 2	4	

Part II—Subtractions from Federal Adjusted Total Income

5.	Enter interest from U.S. government obligations (attach schedule)	5	
6.	Enter subtractions from partnerships, fiduciaries and S corporations (attach schedule)	6	
7.	Other subtractions (attach schedule)	7	
8.	Total subtractions. Enter here and on page 1, line 6	8	

ADDITIONAL INFORMATION REQUIRED

1. Was a Kentucky fiduciary income tax return filed for 2006? ☒ Yes ☐ No. If "No," state reason.

2. If the fiduciary has income not taxed by Kentucky, have you deducted only that portion of expenses allocable to taxable income? ☐ Yes ☒ No. If "Yes," attach computation.
3. Did the estate or trust have any passive activity loss(es)? ☐ Yes ☒ No. (If "Yes," enter the loss(es) on Form 8582-K, Kentucky Passive Activity Loss Limitations, to determine the allowable loss.)
4. If a federal audit changed the taxable income as originally reported for any prior year, a copy of the Revenue Agent's Report must be submitted to the Department of Revenue. Do not attach to this return.
5. During the taxable year did you make an accumulation distribution as defined in Sec. 665(b), Internal Revenue Code? ☐ Yes ☒ No. If "Yes," attach federal Schedule J (Form 1041).
6. If this is an amended return, check the appropriate box on page 1. Explain changes below. Attach a separate page if necessary.

ADDITIONAL EXAMPLES

On the following pages of this manual are three more examples of fiduciary returns. Each example illustrates a particular issue involved in preparing the Kentucky Form 741.

Example 1 is for Snow White Trust. This is a Kentucky Trust with an income adjustment for bonds not taxed at the federal level.

Example 2 is for Chuck E. Cheese Estate. This is a Kentucky estate with adjustments for non taxable income and the pension income exclusion.

Example 3 is for Morticia Adams Estate. This is a non-resident estate with Kentucky partnership income.

The facts and necessary information to complete the Kentucky Form 741 for each follow along with a completed Kentucky Form 741 for each.

FACTS for KENTUCKY FORM 741 EXAMPLE #1

Snow White Trust
Doc Dwarf, Trustee
P O Box 13
Great Forest, Kentucky 40999

Federal Identification Number (FEIN): 61-6199999
Trust beginning date: July 1, 1995

Income Earned in 2007	
Interest From Magic Bank	$ 6,525.00
Interest income from the Sale of Bonds Issued by Kansas	$4,530.00
Dividends from Dopey's Investment, LTD	$ 2,313.00
Capital Gain on 50 shares of Disney Corp	$ 4,300.00
Long-term Capital Loss Carryover	($ 2,550.00)
Kentucky Lottery Winnings	$ 8,000.00
TOTAL	$23,118.00

Deductions incurred in 2007	
Fiduciary Fees Paid	$ 1,150.00
Attorney/Accountant Fees Paid	$ 1,350.00
TOTAL	$ 2,500.00

The total income subject to tax that is reported on Federal Form 1041 of this example equals **$18,588.00**. The interest from the Kansas Bonds ($4,530.00) is not included in the federal total income reported on line 9 of Form 1041. Therefore, the deductions that are reported on federal Form 1041 must be limited to the income reported that is subject to tax.

Total Trust Income	$23,118.00	
Federal Total Income	$18,588.00	81% of total income

The federal income subject to tax is only 81% of ALL income earned. Therefore, only 81% of the deductions paid are allowed on federal Form 1041. The additional 19% of the deductions ($474.00) may be claimed on Kentucky Form 741, line 3 as an additional subtraction. Please note that the $4,530.00 interest earned from the Kansas bonds is reported on Kentucky Form 741, Schedule M, line1.

Form 741
42A741
Department of Revenue

For calendar year or other taxable year beginning ____________ , 2007, and ending ____________ , 2008.

KENTUCKY FIDUCIARY INCOME TAX RETURN 2007

Check applicable box:
- ☐ Decedent's estate
- ☐ Simple trust
- ☐ Complex trust
- ☐ Grantor trust
- ☐ Bankruptcy estate
- ☐ Pooled income fund
- ☐ ____________

Name of Estate or Trust	Snow White Trust
Federal Employer Identification Number	61-6199999
Name and Title of Fiduciary	Doc Dwarf, Trustee
Date Entity Created	7/1/00
Address of Fiduciary (Number and Street or P.O. Box)	P. O. Box 13
Room or Suite Number	
City, State and ZIP Code	Great Forest KY 40999
Telephone Number	(859) 555-5555

Check applicable boxes:
- ☐ Initial return
- ☐ Amended return
- ☐ Final return

Number of Schedules K-1 attached. ➤ ____________ (Copies Must Be Attached)

➤ ***Attach a copy of the federal return including all schedules and statements.***

1.	Federal adjusted total income (federal Form 1041, line 17)	1		16,562
2.	Additions (from page 2, Schedule M, line 4)	2	4,530	
3.	Enter the portion of deductions allocable to line 2	3	474	
4.	Subtract line 3 from line 2	4		4,056
5.	Add lines 1 and 4	5		
6.	Subtractions (from page 2, Schedule M, line 8)	6		
7.	Enter the portion of deductions allocable to line 6	7		
8.	Subtract line 7 from line 6	8		
9.	Subtract line 8 from line 5. This is your Kentucky **adjusted total income (loss)**. Enter here and on page 2, Schedule B, line 1	9		
10.	Income distribution deduction (from page 2, Schedule B, line 15) **(attach Schedule(s) K-1)**	10		
11.	Pension income exclusion (attach Schedule P, if more than $41,110)	11		
12.	Federal estate tax deduction (attach computation)	12		
13.	Add lines 10, 11 and 12	13		
14.	Total income of fiduciary (subtract line 13 from line 9)	14		

INTANGIBLE INCOME ATTRIBUTABLE TO NONRESIDENTS INCLUDED IN LINE 14

15.	**Trusts or estates with income attributable to nonresident beneficiaries.** Enter the portion of intangible income included in line 14 that is attributable to **nonresident beneficiaries.** Enter zero if not applicable. See instructions	15		
16.	Taxable income of fiduciary (subtract line 15 from line 14) **This is your taxable income**	16		

TAX COMPUTATION

17.	Tax: (a) tax rate schedule ________ (b) Form 4972-K ________ (c) Schedule RC-R ________ **Total**	17(d)		
18.	Nonrefundable credit(s) **(specify and attach supporting documents)** ____________	18		
19.	**Enter Tax Credit** *($2 for a trust; $20 for an estate). **This credit is not refundable***	19		
20.	**Total Tax** (subtract lines 18 and 19 from line 17d; if line 18 plus line 19 is more than line 17d, enter -0-)	20		
21.	(a) Estimated tax payments	21(a)		
	(b) Withholding (attach wage and tax statements)	21(b)		
	(c) Refundable Kentucky corporation tax credit (KRS 141.420(3)(c)) **(attach Kentucky Schedule(s) K-1 or Form(s) 725)**	21(c)		
	(d) **Total** (add lines 21(a), (b) and (c))	21(d)		
22.	Subtract line 21(d) from line 20. Enter amount of ☐ tax due ☐ refund ☐ credit forward	22		

I declare under the penalties of perjury that this return (including any accompanying schedules and statements) has been examined by me and, to the best of my knowledge and belief, is a true, correct and complete return.

Signature of Fiduciary or Agent ____ PTIN or Identification Number of Fiduciary or Agent ____ Date ____

Typed or Printed Name of Preparer Other Than Fiduciary or Agent ____ Identification Number of Preparer ____ Date ____

Refunds Mail to: **Kentucky Department of Revenue, Frankfort, KY 40618-0006.**
Payments Mail to: **Kentucky Department of Revenue, Frankfort, KY 40619-0008.**

➤ **Make check payable to: Kentucky State Treasurer.**

SCHEDULE A—CHARITABLE DEDUCTION (Do not complete for a simple trust or pooled income fund.)
Complete Schedule A only if you made additions to or subtractions from total income on page 1, lines 2 or 6 and claimed a charitable deduction on federal Form 1041.

1.	Kentucky taxable income that was paid or set aside for charitable purposes and was not reported on federal Form 1041, Schedule A, including additional capital gains. Enter here and include on Schedule M, line 7	1	
2.	Kentucky tax-exempt income that was paid or set aside for charitable purposes that was reported on federal Form 1041, Schedule A. Enter here and include on Schedule M, line 3	2	

SCHEDULE B—INCOME DISTRIBUTION DEDUCTION (See federal instructions.)

1.	Adjusted total income (enter amount from page 1, line 9)	1	
2.	Adjusted tax-exempt interest	2	
3.	Net gain shown on Schedule D, Form 741, column 1, line 17 (if net loss, enter zero)	3	
4.	Enter amount included from federal Schedule A, line 4	4	
5.	Enter net capital gains included on Kentucky Schedule A, line 1 or line 2	5	
6.	Enter any Kentucky gains included on page 1, line 9 as a negative figure. If capital loss, enter as a positive figure. (Kentucky gain/loss includes federal figures plus Kentucky adjustments.)	6	
7.	**Distributable net income** (combine lines 1 through 6)	7	
8.	If complex trust, enter accounting income for tax years as determined under the governing instrument and applicable law	8	
9.	Amount of income required to be distributed currently	9	
10.	Other amounts paid, credited or otherwise required to be distributed	10	
11.	Total distributions (add lines 9 and 10) (If greater than line 8, see federal instructions.)	11	
12.	Enter the amount of tax-exempt income included on line 11	12	
13.	Tentative income distribution deduction (subtract line 12 from line 11)	13	
14.	Tentative income distribution deduction (subtract line 2 from line 7)	14	
15.	**Income distribution deduction** (enter the smaller of line 13 or line 14 here and on page 1, line 10)	15	

SCHEDULE M (FORM 741)

	Part I—Additions to Federal Adjusted Total Income		
1.	Enter interest from bonds issued by other states and their political subdivisions	1	4,530
2.	Enter additions from partnerships, fiduciaries and S corporations (attach schedule)	2	
3.	Other additions (attach schedule)	3	
4.	Total additions. Enter here and on page 1, line 2	4	4,530
	Part II—Subtractions from Federal Adjusted Total Income		
5.	Enter interest from U.S. government obligations (attach schedule)	5	
6.	Enter subtractions from partnerships, fiduciaries and S corporations (attach schedule)	6	
7.	Other subtractions (attach schedule)	7	
8.	Total subtractions. Enter here and on page 1, line 6	8	

ADDITIONAL INFORMATION REQUIRED

1. Was a Kentucky fiduciary income tax return filed for 2006? ☐ Yes ☐ No. If "No," state reason.

____

____

2. If the fiduciary has income not taxed by Kentucky, have you deducted only that portion of expenses allocable to taxable income? ☐ Yes ☐ No. If "Yes," attach computation.
3. Did the estate or trust have any passive activity loss(es)? ☐ Yes ☐ No. (If "Yes," enter the loss(es) on Form 8582-K, Kentucky Passive Activity Loss Limitations, to determine the allowable loss.)
4. If a federal audit changed the taxable income as originally reported for any prior year, a copy of the Revenue Agent's Report must be submitted to the Department of Revenue. Do not attach to this return.
5. During the taxable year did you make an accumulation distribution as defined in Sec. 665(b), Internal Revenue Code? ☐ Yes ☐ No. If "Yes," attach federal Schedule J (Form 1041).
6. If this is an amended return, check the appropriate box on page 1. Explain changes below. Attach a separate page if necessary.

____

____

FACTS for KENTUCKY FORM 741 EXAMPLE #2

Chuck E. Cheese Estate
Mia Pizza, Executrix
963 Kiddie Lane
Token, Kentucky 41111

Federal Identification Number (FEIN): 61-2000000
Estate beginning date: July 1, 2007

Income Earned in 2007	
Interest From Maniac Bank	$ 4,925.00
Interest from US Treasury Bonds	$ 4,515.00
Dividends from Pepperoni Investments	$ 2,616.00
Capital Gain on 50 shares of Mozzarella Corp	$ 5,500.00
Long-term Capital Loss Carryover	($ 2,550.00)
Pension/Annuity Income	$22,500.00
TOTAL	$37,506.00

Deductions incurred in 2007	
Fiduciary Fees Paid	$ 1,830.00
Attorney/Accountant Fees Paid	$ 2,250.00
TOTAL	$ 4,080.00

The total income is $37,506.00. All of this income is taxable on federal Form 1041.

The interest from the US Treasury Bonds is not taxable on Kentucky Form 741. This is subtracted on Form 741, Schedule M, Line 5. The annuity income received is not taxable to Kentucky due to the allowable pension income exclusion. This amount is subtracted on Form 741, line 11. (The estate in this example receives the pension income exclusion, as the estate is to pay all taxes.)

The total income that is taxable to Kentucky is $10,491.00 ($4,925.00 interest + $2,616.00 dividends + $2,950.00 capital gain). The Kentucky income is less than the total income and, therefore, the deductions allowed on the Kentucky return must be prorated based on the Kentucky income to the total income.

$$\$10{,}491.00 \div \$37{,}506.00 = 28\%$$

28% of the $4,080.00 deductions equals $1,142.00. That is the allowable deduction for Kentucky. As a result, the difference of $2,938.00 must be added on line 7 of Form 741.

Form 741
42A741
Department of Revenue
For calendar year or other taxable year
beginning ____________ , 2007, and ending ____________ , 2008.

Kentucky

KENTUCKY FIDUCIARY INCOME TAX RETURN **2007**

Check applicable box:
- [x] Decedent's estate
- [ ] Simple trust
- [ ] Complex trust
- [ ] Grantor trust
- [ ] Bankruptcy estate
- [ ] Pooled income fund
- [ ] ________________

Name of Estate or Trust	Federal Employer Identification Number
Chuck E. Cheese Estate	61-2000000
Name and Title of Fiduciary	Date Entity Created
Mia Pizza, Executrix	7/1/07
Address of Fiduciary (Number and Street or P.O. Box)	Room or Suite Number
963 Kiddie Lane	
City, State and ZIP Code	Telephone Number
Token KY 41111	

Check applicable boxes:
- [ ] Initial return
- [ ] Amended return
- [ ] Final return

Number of Schedules K-1 attached. ➤ ___________ **(Copies Must Be Attached)**

➤ ***Attach a copy of the federal return including all schedules and statements.***

1.	Federal adjusted total income (federal Form 1041, line 17) ... 1		33,426
2.	Additions (from page 2, Schedule M, line 4) ... 2		
3.	Enter the portion of deductions allocable to line 2 ... 3		
4.	Subtract line 3 from line 2 ... 4		
5.	Add lines 1 and 4 ... 5		33,426
6.	Subtractions (from page 2, Schedule M, line 8) ... 6	4,515	
7.	Enter the portion of deductions allocable to line 6 ... 7	2,938	
8.	Subtract line 7 from line 6 ... 8		1,577
9.	Subtract line 8 from line 5. This is your Kentucky **adjusted total income (loss)**. Enter here and on page 2, Schedule B, line 1 ... 9		31,849
10.	Income distribution deduction (from page 2, Schedule B, line 15) **(attach Schedule(s) K-1)** ... 10		
11.	Pension income exclusion (attach Schedule P, if more than $41,110) ... 11	22,500	
12.	Federal estate tax deduction (attach computation) ... 12		
13.	Add lines 10, 11 and 12 ... 13		22,500
14.	Total income of fiduciary (subtract line 13 from line 9) ... 14		9,349

INTANGIBLE INCOME ATTRIBUTABLE TO NONRESIDENTS INCLUDED IN LINE 14

15.	**Trusts or estates with income attributable to nonresident beneficiaries.** Enter the portion of intangible income included in line 14 that is attributable to **nonresident beneficiaries.** Enter zero if not applicable. See instructions ... 15		
16.	Taxable income of fiduciary (subtract line 15 from line 14) **This is your taxable income** ... 16		

TAX COMPUTATION

17.	Tax: (a) tax rate schedule ________ (b) Form 4972-K ________ (c) Schedule RC-R ________ **Total** 17(d)		
18.	Nonrefundable credit(s) **(specify and attach supporting documents)** ________ ... 18		
19.	Enter **Tax Credit** *($2 for a trust; $20 for an estate). This credit is not refundable* ... 19		
20.	**Total Tax** (subtract lines 18 and 19 from line 17d; if line 18 plus line 19 is more than line 17d, enter -0-) ... 20		
21.	(a) Estimated tax payments ... 21(a)		
	(b) Withholding (attach wage and tax statements) ... 21(b)		
	(c) Refundable Kentucky corporation tax credit (KRS 141.420(3)(c)) **(attach Kentucky Schedule(s) K-1 or Form(s) 725)** ... 21(c)		
	(d) **Total** (add lines 21(a), (b) and (c)) ... 21(d)		
22.	Subtract line 21(d) from line 20. Enter amount of ☐ tax due ☐ refund ☐ credit forward ... 22		

I declare under the penalties of perjury that this return (including any accompanying schedules and statements) has been examined by me and, to the best of my knowledge and belief, is a true, correct and complete return.

Signature of Fiduciary or Agent | PTIN or Identification Number of Fiduciary or Agent | Date

Typed or Printed Name of Preparer Other Than Fiduciary or Agent | Identification Number of Preparer | Date

Refunds Mail to: **Kentucky Department of Revenue, Frankfort, KY 40618-0006.**
Payments Mail to: **Kentucky Department of Revenue, Frankfort, KY 40619-0008.**

➤ **Make check payable to: Kentucky State Treasurer.**

SCHEDULE A—CHARITABLE DEDUCTION (Do not complete for a simple trust or pooled income fund.)

Complete Schedule A only if you made additions to or subtractions from total income on page 1, lines 2 or 6 and claimed a charitable deduction on federal Form 1041.

1. Kentucky taxable income that was paid or set aside for charitable purposes and was not reported on federal Form 1041, Schedule A, including additional capital gains. Enter here and include on Schedule M, line 7	1	
2. Kentucky tax-exempt income that was paid or set aside for charitable purposes that was reported on federal Form 1041, Schedule A. Enter here and include on Schedule M, line 3	2	

SCHEDULE B—INCOME DISTRIBUTION DEDUCTION (See federal instructions.)

1. Adjusted total income (enter amount from page 1, line 9)	1	
2. Adjusted tax-exempt interest	2	
3. Net gain shown on Schedule D, Form 741, column 1, line 17 (if net loss, enter zero)	3	
4. Enter amount included from federal Schedule A, line 4	4	
5. Enter net capital gains included on Kentucky Schedule A, line 1 or line 2	5	
6. Enter any Kentucky gains included on page 1, line 9 as a negative figure. If capital loss, enter as a positive figure. (Kentucky gain/loss includes federal figures plus Kentucky adjustments.)	6	
7. **Distributable net income** (combine lines 1 through 6)	7	
8. If complex trust, enter accounting income for tax years as determined under the governing instrument and applicable law	8	
9. Amount of income required to be distributed currently	9	
10. Other amounts paid, credited or otherwise required to be distributed	10	
11. Total distributions (add lines 9 and 10) (If greater than line 8, see federal instructions.)	11	
12. Enter the amount of tax-exempt income included on line 11	12	
13. Tentative income distribution deduction (subtract line 12 from line 11)	13	
14. Tentative income distribution deduction (subtract line 2 from line 7)	14	
15. **Income distribution deduction** (enter the smaller of line 13 or line 14 here and on page 1, line 10)	15	

SCHEDULE M (FORM 741)

Part I—Additions to Federal Adjusted Total Income		
1. Enter interest from bonds issued by other states and their political subdivisions	1	
2. Enter additions from partnerships, fiduciaries and S corporations (attach schedule)	2	
3. Other additions (attach schedule)	3	
4. Total additions. Enter here and on page 1, line 2	4	
Part II—Subtractions from Federal Adjusted Total Income		
5. Enter interest from U.S. government obligations (attach schedule)	5	4,515
6. Enter subtractions from partnerships, fiduciaries and S corporations (attach schedule)	6	
7. Other subtractions (attach schedule)	7	
8. Total subtractions. Enter here and on page 1, line 6	8	4,515

ADDITIONAL INFORMATION REQUIRED

1. Was a Kentucky fiduciary income tax return filed for 2006? ☐ Yes ☐ No. If "No," state reason.

____

____

2. If the fiduciary has income not taxed by Kentucky, have you deducted only that portion of expenses allocable to taxable income? ☐ Yes ☐ No. If "Yes," attach computation.
3. Did the estate or trust have any passive activity loss(es)? ☐ Yes ☐ No. (If "Yes," enter the loss(es) on Form 8582-K, Kentucky Passive Activity Loss Limitations, to determine the allowable loss.)
4. If a federal audit changed the taxable income as originally reported for any prior year, a copy of the Revenue Agent's Report must be submitted to the Department of Revenue. Do not attach to this return.
5. During the taxable year did you make an accumulation distribution as defined in Sec. 665(b), Internal Revenue Code? ☐ Yes ☐ No. If "Yes," attach federal Schedule J (Form 1041).
6. If this is an amended return, check the appropriate box on page 1. Explain changes below. Attach a separate page if necessary.

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FACTS FOR KENTUCKY FORM 741 EXAMPLE # 3

Morticia Adams Estate
Wednesday Adams, Executrix
1313 Old Mansion Way
Beverly Hills, California 90210

FEIN: 61-0000003
Estate begins date of death: August 30, 2007

Income Earned in 2007	
Interest Received	$ 225.00
Ordinary Dividends	$ 1,269.00
Capital Gains	$12,216.00
Partnership Distribution (KY)	$19,533.00
TOTAL	$33,243.00

Deductions for tax year 2007	
Investment Interest	$ 325.00
Fiduciary Fees	$2,820.00
Attorney & Accountant Fees	$4,150.00
TOTAL	$7,295.00

Morticia Adams died in California of old age. She had always been a resident of California. She was a partner in Transylvania Unlimited LLP, a Kentucky partnership and received distributions of income from this Kentucky partnership. Her estate received the income distributions after the date of her death. These distributions will be reported on Kentucky Form 741. Please review the information and completed forms for this non resident estate example on the following pages.

The federal adjusted total income from Form 1041, Line 17, is to be reported on Line 1 of the Kentucky Form 741. However, only the Kentucky Partnership distribution income is subject to Kentucky tax. An amount of $19,533.00 was distributed from the Kentucky partnership. (The Kentucky partnership did not receive interest and dividends.) Therefore, we need to complete the Form 741 to reflect only the Kentucky income and deductions attributable to the Kentucky income.

Kentucky Income	$19,533
Total Income	$33,243

The difference in income that must be subtracted from the Form 741, Schedule M, Line 7 is $13,710.00. This amount is also entered on Form 741, page 1, Line 6.

A supplemental schedule indicating the subtraction due to the estate's non residency should be attached to the Form 741.

Likewise, the deductions allowed against this income must be prorated based on Kentucky income subject to tax and total income. The percentage of Kentucky to Total Income is 59%.

$7,295 (deductions) X 59% = $4,304

The difference of $2,991 ($7,295 - $4,304) of deductions not attributable to the Kentucky income must be reported on Form 741, page 1, Line 7.

Therefore, the Kentucky adjusted total income is computed to be $15,229.00.

Note: To double check your calculations in this example compare the Kentucky income minus allowable deductions to the Kentucky adjusted total income on Line 9, Page 1 of Form 741:

Partnership Income Attributable to Kentucky:	$19,533
Minus the deductions attributable to this Kentucky Income:	4,304
Total KY adjusted income =	$15,229

Form 741
42A741
Department of Revenue

For calendar year or other taxable year beginning 8/30, 2007, and ending 12/31, 2008.

KENTUCKY FIDUCIARY INCOME TAX RETURN 2007

Check applicable box:
- ☒ Decedent's estate
- ☐ Simple trust
- ☐ Complex trust
- ☐ Grantor trust
- ☐ Bankruptcy estate
- ☐ Pooled income fund
- ☐ ____________

Name of Estate or Trust	Federal Employer Identification Number
Morticia Adams Estate	61-0000003
Name and Title of Fiduciary	**Date Entity Created**
Wednesday Adams, Executrix	8/30/07
Address of Fiduciary (Number and Street or P.O. Box)	**Room or Suite Number**
1313 Old Mansion Way	
City, State and ZIP Code	**Telephone Number**
Beverly Hills CA 90210	

Check applicable boxes:
- ☒ Initial return
- ☐ Amended return
- ☐ Final return

Number of Schedules K-1 attached. ➤ 2 **(Copies Must Be Attached)**

➤ ***Attach a copy of the federal return including all schedules and statements.***

1.	Federal adjusted total income (federal Form 1041, line 17) ... 1		25,948
2.	Additions (from page 2, Schedule M, line 4) ... 2		
3.	Enter the portion of deductions allocable to line 2 ... 3		
4.	Subtract line 3 from line 2 ... 4		
5.	Add lines 1 and 4 ... 5		25,948
6.	Subtractions (from page 2, Schedule M, line 8) ... 6	13,710	
7.	Enter the portion of deductions allocable to line 6 ... 7	2,991	
8.	Subtract line 7 from line 6 ... 8		10,719
9.	Subtract line 8 from line 5. This is your Kentucky **adjusted total income (loss)**. Enter here and on page 2, Schedule B, line 1 ... 9		15,229
10.	Income distribution deduction (from page 2, Schedule B, line 15) **(attach Schedule(s) K-1)** ... 10		
11.	Pension income exclusion (attach Schedule P, if more than $41,110) ... 11		
12.	Federal estate tax deduction (attach computation) ... 12		
13.	Add lines 10, 11 and 12 ... 13		
14.	Total income of fiduciary (subtract line 13 from line 9) ... 14		
	INTANGIBLE INCOME ATTRIBUTABLE TO NONRESIDENTS INCLUDED IN LINE 14		
15.	**Trusts or estates with income attributable to nonresident beneficiaries.** Enter the portion of intangible income included in line 14 that is attributable to **nonresident beneficiaries.** Enter zero if not applicable. See instructions ... 15		
16.	Taxable income of fiduciary (subtract line 15 from line 14) **This is your taxable income** ... 16		
	TAX COMPUTATION		
17.	Tax: (a) tax rate schedule ______ (b) Form 4972-K ______ (c) Schedule RC-R ______ **Total** 17(d)		
18.	Nonrefundable credit(s) **(specify and attach supporting documents)** ______ ... 18		
19.	Enter **Tax Credit** *($2 for a trust; $20 for an estate). **This credit is not refundable*** ... 19		
20.	**Total Tax** (subtract lines 18 and 19 from line 17d; if line 18 plus line 19 is more than line 17d, enter -0-) ... 20		
21.	(a) Estimated tax payments ... 21(a)		
	(b) Withholding (attach wage and tax statements) ... 21(b)		
	(c) Refundable Kentucky corporation tax credit (KRS 141.420(3)(c)) **(attach Kentucky Schedule(s) K-1 or Form(s) 725)** ... 21(c)		
	(d) **Total** (add lines 21(a), (b) and (c)) ... 21(d)		
22.	Subtract line 21(d) from line 20. Enter amount of ☐ tax due ☐ refund ☐ credit forward ... 22		

I declare under the penalties of perjury that this return (including any accompanying schedules and statements) has been examined by me and, to the best of my knowledge and belief, is a true, correct and complete return.

Signature of Fiduciary or Agent — PTIN or Identification Number of Fiduciary or Agent — Date

Typed or Printed Name of Preparer Other Than Fiduciary or Agent — Identification Number of Preparer — Date

Refunds Mail to: **Kentucky Department of Revenue, Frankfort, KY 40618-0006.**
Payments Mail to: **Kentucky Department of Revenue, Frankfort, KY 40619-0008.**

➤ **Make check payable to: Kentucky State Treasurer.**

SCHEDULE A—CHARITABLE DEDUCTION (Do not complete for a simple trust or pooled income fund.)
Complete Schedule A only if you made additions to or subtractions from total income on page 1, lines 2 or 6 and claimed a charitable deduction on federal Form 1041.

1. Kentucky taxable income that was paid or set aside for charitable purposes and was not reported on federal Form 1041, Schedule A, including additional capital gains. Enter here and include on Schedule M, line 7	1	
2. Kentucky tax-exempt income that was paid or set aside for charitable purposes that was reported on federal Form 1041, Schedule A. Enter here and include on Schedule M, line 3	2	

SCHEDULE B—INCOME DISTRIBUTION DEDUCTION (See federal instructions.)

1. Adjusted total income (enter amount from page 1, line 9)	1	
2. Adjusted tax-exempt interest	2	
3. Net gain shown on Schedule D, Form 741, column 1, line 17 (if net loss, enter zero)	3	
4. Enter amount included from federal Schedule A, line 4	4	
5. Enter net capital gains included on Kentucky Schedule A, line 1 or line 2	5	
6. Enter any Kentucky gains included on page 1, line 9 as a negative figure. If capital loss, enter as a positive figure. (Kentucky gain/loss includes federal figures plus Kentucky adjustments.)	6	
7. **Distributable net income** (combine lines 1 through 6)	7	
8. If complex trust, enter accounting income for tax years as determined under the governing instrument and applicable law	8	
9. Amount of income required to be distributed currently	9	
10. Other amounts paid, credited or otherwise required to be distributed	10	
11. Total distributions (add lines 9 and 10) (If greater than line 8, see federal instructions.)	11	
12. Enter the amount of tax-exempt income included on line 11	12	
13. Tentative income distribution deduction (subtract line 12 from line 11)	13	
14. Tentative income distribution deduction (subtract line 2 from line 7)	14	
15. **Income distribution deduction** (enter the smaller of line 13 or line 14 here and on page 1, line 10)	15	

SCHEDULE M (FORM 741)

Part I—Additions to Federal Adjusted Total Income		
1. Enter interest from bonds issued by other states and their political subdivisions	1	
2. Enter additions from partnerships, fiduciaries and S corporations (attach schedule)	2	
3. Other additions (attach schedule)	3	
4. Total additions. Enter here and on page 1, line 2	4	
Part II—Subtractions from Federal Adjusted Total Income		
5. Enter interest from U.S. government obligations (attach schedule)	5	
6. Enter subtractions from partnerships, fiduciaries and S corporations (attach schedule)	6	
7. Other subtractions (attach schedule)	7	13,710
8. Total subtractions. Enter here and on page 1, line 6	8	13,710

ADDITIONAL INFORMATION REQUIRED

1. Was a Kentucky fiduciary income tax return filed for 2006?
☐ Yes ☐ No. If "No," state reason.

____

____

2. If the fiduciary has income not taxed by Kentucky, have you deducted only that portion of expenses allocable to taxable income? ☐ Yes ☐ No. If "Yes," attach computation.
3. Did the estate or trust have any passive activity loss(es)? ☐ Yes ☐ No. (If "Yes," enter the loss(es) on Form 8582-K, Kentucky Passive Activity Loss Limitations, to determine the allowable loss.)
4. If a federal audit changed the taxable income as originally reported for any prior year, a copy of the Revenue Agent's Report must be submitted to the Department of Revenue. Do not attach to this return.
5. During the taxable year did you make an accumulation distribution as defined in Sec. 665(b), Internal Revenue Code? ☐ Yes ☐ No. If "Yes," attach federal Schedule J (Form 1041).
6. If this is an amended return, check the appropriate box on page 1. Explain changes below. Attach a separate page if necessary.

____

____

FAQ'S, NOTES & MORE

Q. Can a fiduciary return be filed electronically?
A. No.

Q. How can a fiduciary return be amended?
A. Use form 741, mark the amended check box and complete with the corrected figures.

Q. Can a fiduciary file for an extension?
A. Yes. A fiduciary can qualify for a 6 month extension, same as Individual.
.
Q. What is the due date for a fiduciary income tax return?
A. Trust returns are due on April 15th. Trusts are required to file on a calendar year. Estate returns are due on April 15th if a calendar year is chosen. Otherwise, the due date is three-and-a-half months from the close of the fiscal year elected.

Q. Can fiduciaries file as a fiscal year filer?
A. Estates may, but trusts can file as a calendar year filer only.

Q. Are fiduciaries allowed to take a credit for tax paid to another state?
A. Yes. However, credit may be limited to tax paid or tax savings if income omitted on the return.

Q. Can fiduciaries take a standard deduction.
A. No.

Q. Can fiduciaries itemize deductions?
A. No. Items that would be itemized are accounted for within the return.

Q. Can fiduciaries take the Family Size Tax Credit?
A. No.

Q. What is the tax rate for fiduciaries?
A. Fiduciaries are taxed at the same rate as individuals.

Q. Can fiduciaries claim a Net Operating Loss
A. Yes.

Q. Are the attorney and accountant fees allowed on the fiduciary income tax return if the same fees are claimed as an expense on the federal estate return?

A. No. The attorney and accountant fees paid may be claimed on one type tax or the other, but not both. A double deduction cannot be claimed. A statement must be attached to the Kentucky Form 741 stating that the fees have not been claimed previously.

Q. Are nonresident beneficiaries required to pay Kentucky tax on their distribution from a fiduciary?

A. Yes, if the income is from tangible or business property located in Kentucky. No, if the income is intangible. (These are the same as Individual Income Tax laws.)

Q. If a percentage of the beneficiaries are nonresidents to Kentucky and the tax is being paid on the fiduciary level (as compared to being reported in the Schedule K-1 and being taxed on the beneficiary level), is all level income taxed, including intangible income?

A. No. The intangible income attributable to the nonresidents is tax-exempt. This amount of exempt income should be reported on the Kentucky Form 741, line 15. Line 15 of the Form 741 is to be used only for this type of income that is tax-exempt to Kentucky.

Q. If all the income has been distributed and reported on the Kentucky Schedule K-1, what amount is to be entered on Form 741, Line 15?

A. None. If all income is being distributed and reported on the Kentucky Schedule K-1, no income exists that is being taxed on the fiduciary level, i.e., no income is being computed on the Form 741.

Q. What number is used on the form for the taxpayer ID?

A. Estates may use either the Individual's Social Security number or FEIN, if available. Trusts will use the FEIN.

Q. Is an IRA distribution taxable on the Kentucky Form 741?

A. Yes. IF the IRA distribution goes directly to the estate or trust and not directly to a certain individual or individuals, then the IRA distribution must be reported on the Kentucky Form 741.

Q. Is the allowable amount of pension exclusion claimed on the fiduciary income tax return or by the beneficiaries ?

A. The allowable pension and annuity exclusion is claimed on the Kentucky Form 741 if the pension/annuity is being taxed on the fiduciary income tax return. If the pension/annuity is being distributed and reported on the Schedule K-1, the allowable exclusion may be claimed on the individual beneficiary(ies) Kentucky income tax return.

QUICK NOTES & FACTS

Account Number The Department of Revenue does not currently assign identification numbers to estates or trusts.

Bankruptcy Estates: The income and deductions are actually reported and tax calculated on the individual income tax return and the tax amount is the reported on the Fiduciary income tax return. A complete copy of the individual income tax return reporting the income and deductions must be attached to the Form 741.

Capital Gains Different tax rates may apply to capital gain income for federal purposes. Kentucky taxes capital gain income as ordinary income. Capital gain is taxed to the estate or trust where the gain must be or is added to principal. However, when the gain is actually distributed to beneficiaries during the tax year, it is included in the computation of distributable net income and, therefore, is taxed to the beneficiary.

Charitable Deductions Charitable deductions are not limited to the amount of adjusted gross income reported on the fiduciary income tax return, as individual taxpayers are required to do. Estates and complex trusts are allowed an unlimited charitable deduction for amounts that are paid to recognized charities out of gross income during a tax year. The amounts paid must be set by the terms of the will or trust instrument

Federal fiduciary tax Do not include federal fiduciary tax paid on Form 1041 or Kentucky Form 741; this is not an allowable deduction.

Fiscal/Calendar: A trust may only file on a calendar year basis.

K-1's The fiduciary must file Schedule K-1 to report any income distribution deduction claimed. A copy of each beneficiary's Schedule K-1 is attached to the Form 741. The number of Schedules K-1 attached should be indicated on the front of the Form 741 below the name and address area.

Nonresident Trusts & Estates Nonresident trusts are not required to file Kentucky Form 741 unless income is received from Kentucky sources.

A trust is considered to be a Kentucky trust if the principal place of administration of the trust takes place in Kentucky.

Nonresident estates and trusts are not taxed on intangible income received from Kentucky sources, based on the laws also applicable to individual income tax.

Pension Exclusion Kentucky's pension income exclusion is available for the fiduciary if the fiduciary retains the income. If pension income is distributed to the beneficiary(ies) then the pension income exclusion is available to the beneficiary.

Simple/Complex: A trust can never be a simple trust during the year of termination or in a year of partial liquidation.

Split Interest Trusts Filing: Form 5227, Split-Interest Trust Information Return must be filed for the pooled income fund/split interest trust and attached to Form 741 with demographics entered only.

Standard Deduction The standard deduction permitted individuals in KRS 141.080 is not allowed for estates or trusts.

Unallowable Deductions To compute unallowable deductions, divide the Kentucky tax-exempt income by the total income of the fiduciary. Multiply total deductions by this percentage.

FOR REFERENCE: ADDITIONAL INFORMATION ON SELECTED ISSUES

Allocation of Estimated Taxes to Beneficiaries: A trustee or executor may elect to allocate any portion of the estimated tax payments to any beneficiary. The allocation election is available for an estate only for its final tax year. The fiduciary makes the election by (1) completing and filing Form 1041-T and (2) completing Line 14a of Schedule K-1 for each beneficiary to whom the estimated tax payments are allocated. A trust's or estate's election must be filed on or before the 65th day after the close of its tax year otherwise it will be considered invalid (Code Sec. 643(g)). For calendar tax year 2005, Form 1041-T must be filed on or before March 7, 2006. Form 1041-T should be attached to Form 1041 only if the election is made before Form 1041 is filed. Otherwise, Form 1041-T is signed and filed separately.

CAPITAL GAINS AND LOSSES: Gains and losses from the sale or exchange of capital assets are computed on Parts I and II of Schedule D, Form 1041 and allocated between the fiduciary and the beneficiaries on Part III of Schedule D, Form 1041. Capital assets are defined in Instructions for Form 1041.

The maximum capital gain rate is generally 10% for estates and trusts that would be taxed at the 15% rate on ordinary income. A 15% maximum tax rate replaces the 20% rate and a 5% maximum rate replaces the 10% rate that existed under prior law.

A 25% rate applies to unrecaptured section 1250 gain (i.e., unrecaptured depreciation) from the sale, exchange, etc., of depreciable real estate if the property was held for more than one year. Unrecaptured section 1250 gain is computed on a worksheet provided in the Form 1041 instructions.

A 28% rate applies to long-term collectibles gain and the amount of gain equal to the exclusion claimed for qualified small business stock under Code Sec. 1202. (Fifty percent of qualified small business stock gain is exempt from tax; the remaining gain is treated as 28% rate gain.)

Property acquired by a decedent's estate from a decedent is considered held for more than 12 months (Code Sec. 1223(11)). The short and long-term carryover amounts entered on Lines 4 and 11 are determined using the capital loss carryover worksheet contained in the Form 1041 instructions.

Part III of Schedule D is used to show the allocation of the net short term capital gain or loss reported on Line 5 and the net long-term capital gain or loss reported on Line 12 between the estate or trust and the beneficiaries as a group. The amount allocated to each beneficiary is shown on each beneficiary's Schedule K-1.

The beneficiaries' share of net short-term capital gain or loss is reported on Line 13, column 1, Part III. The estate or trust's share is reported in column 2. Net long-term capital gain is allocated between the beneficiaries and estate or trust on Line 14a, columns 1 and 2, respectively. Twenty-eight percent rate gain or loss and unrecaptured section 1250 gain are identified separately on Lines 14(b) and 14(c), respectively. Each beneficiary's share of net capital gain is reported on Schedule K-l as follows: net short-term capital gains, Line 3; total net long-term capital gains, Line 4a; unrecaptured section 1250 gain, Line 4b; and long-term capital gain subject to the 28% rate, Line 4c.

Capital gain may only be allocated to beneficiaries to the extent that it is considered as paid, credited, or required to be distributed to any beneficiary during the tax year (Reg. §i.643(a)-3(a)). Similarly, capital losses are taken into account only to the extent that they enter into the determination of any capital gains that are paid, credited, or required to be distributed to any beneficiary during the tax year (Reg. §l.643(a)(3)-3(b)).

Generally, capital gain is considered paid, credited, or required to be distributed to a beneficiary only if it is:

(1) allocated to income under the terms of the governing instrument or local law;

(2) allocated to corpus and actually distributed to beneficiaries; or

(3) utilized (pursuant to the terms of the governing instrument or the practice followed by the fiduciary) in determining the amount distributed or required to be distributed to the beneficiaries (Reg. §l.643(a)(3)-3(b))

Any capital gain paid or permanently set aside for a charitable purpose specified in Code Sec. 642(c) must be allocated to the estate or trust in column 2 (Reg. §l.643(a)-3).

Except for the year in which an estate or trust terminates, if there is a net short-term capital loss from the sale or exchange of capital assets on Line 5, the entire net loss must be allocated to the estate or trust (Reg. §1.642(h)-l). Similarly, a net long-term capital loss on Line 13 of schedule D must be allocated entirely to the estate or trust.

Part IV is completed to determine the capital loss limitation (the smaller of the loss reported on Line 15, column (3) or $3,000) if a total net loss is reported on Line 15, column 3. If the Line 15, column (3) loss is greater than $3,000 (or a negative taxable income (net operating loss) is reported on Line 22 of Form 1041) the capital loss carryover worksheet contained in the instructions should be completed.

In the final year of a trust or decedent's estate, short- term and long-term capital loss carryovers may be claimed by the beneficiaries on Schedule K-1, Lines 13b and 13c, respectively.

Part V of Schedule D applies the appropriate tax rates to net long-term gain reported elsewhere on the schedule. A short-term or long-term capital loss carryover is reported on Line 4 or

CASUALTY OR THEFT GAIN OR LOSS: Gains and losses from casualties and thefts of property are reported item-by-item on Form 4684, Casualties and Thefts, in either Section A (for property not used in a trade or business or for income-producing purposes) or Section B (for property used in a trade or business or for income-producing purposes). Nonbusiness losses are deductible only to the extent that the total amount of such losses, after a $100 reduction for each casualty or theft, exceeds 10% of a taxpayer's adjusted gross income.

Casualty and theft losses are allowable to an estate only if the loss has not been claimed as a deduction from the gross estate of the decedent in a federal estate tax return.

Section B, Part II, of Form 4684, which deals with property used in a trade or business or for income- producing purposes, separates casualty and theft gains and losses into two general types. The first involves such gains and losses on short-term property. Net gains of this type are taxed as ordinary income, and net losses are treated as ordinary losses. The second type involves such gains and losses on long- term property. Net gains from this type of property qualify for Sec. 1231 (capital gain) treatment, and net losses are treated as ordinary losses. The gains and losses reported on Form 4684 may be reported directly on page 1 of Form 1041 and on Schedule D of Form 1041, or on Form 4797 in accordance with the following rules:

1. *Casualty or theft of property held short term (Form 4684, Section B, Part If, Lines* 29—32).——Short-term casually and theft gains and losses are separated into (1) losses involving trade, business, rental or royalty property (column (b)(i)), (2) losses involving income-producing property (column b)(il)), and (3) gains from casualties and thefts includible in income (column (c)). The net gain or loss from combining columns (b)(i) and (c) of Line 30 is an ordinary gain or loss and is transferred to Line 14, Part II, Form 4797. However, if Form 4797 does not otherwise have to be filed, the net gain or loss is reported on Line 7, page 1, Form 1041, with the notation "Form 4684." Total losses from other property (column (b)(ii), Line 30) are entered on Line 32 of Form 4684 and are then deducted as "other deductions" on Line 15a, page 1, Form 1041.

2. *Casualty or theft of property held long term (Form 4684, Section B, Part II, Lines* 33—39)—In Part II, long-term casualty and theft gains and losses are also categorized into losses involving trade or business, etc., property, losses from income-producing property, and gains from casualties or thefts includible in income. The gain from recapture property from Form 4797 is reflected in the computation. A net loss from Line

38a is transferred to Line 14, Part II, Form 4797, where it becomes part of the ordinary gain and loss computation.

If Form 4797 does not otherwise have to be filed, the net loss from Line 38a is reported on Line 7, page 1, Form 1041, with the notation "Form 4684." In addition, total losses from income-producing property (Line 35, Form 4684, column (b)(ii)) are entered on Line 38b and then are deducted on Line ISa, page 1, Form 1041. However, if the netting of total gains on Line 36 against the total losses on Line 3? produces a net gain, the net gain is reported on Line 39 and is treated as a capital gain. The net gain, as reported on Line 39, is carried to Line 3, Part I, Form 4797, where it becomes part of the capital gain-ordinary loss computation.

CEMETERY PERPETUAL CARE FUND: On Line 18, page 1, of Form 1041, the amount paid for the maintenance of cemetery property (limited to $5 per gravesite) may be deducted. The number of gravesites should be entered to the right of the entry space for Line 18. Also, "(Section 642(i) Trust)" should be written after the trust's name at the top of Form 1041. It is not necessary to complete Schedules B and K-1 for a cemetery perpetual care fund.

PASSIVE ACTIVITY LOSS AND CREDIT LIMITATIONS: Losses derived from passive activities are limited to the amount of income derived from all passive activities conducted by the estate or the trust (Code Sec. 469). Similarly, tax credits from passive activities are limited to the tax liability generated by the passive activities. These limitations are first applied at the estate or trust level.

Generally a passive activity is one that involves the conduct of a trade or business in which the taxpayer does not materially participate. While rental activities are generally considered passive activities, rental real estate activities are not subject to passive loss limitations for certain taxpayers who materially participate in real property trades and businesses (Code Sec. 469(c)(7)). In the case of a grantor trust, material participation is determined by reference to the activities conducted by the grantor. The IRS has not released guidelines for determining what constitutes material participation for an estate or nongrantor trust (Temp. Reg. §1.469-5T(g)).

Portfolio income received by an estate or trust (interest, dividends, royalties, annuity income (Code Sec. 469(e)) is not treated as income derived from a passive activity. Similarly, income derived from a working interest in oil and gas property is not income from a passive activity (Code Sec. 469(c)(3)).

An estate can deduct up to $25,000 in rental real estate activity expenses incurred in tax years ending within two years after the decedent's death, provided that the decedent actively participated in the activity (Code Sec. 469(i)(4)). Any unused losses or credits are suspended and are carried forward indefinitely. Also, if an estate or trust distributes an interest in a passive activity, the basis of the property immediately before the distribution is increased by passive losses allocable to the interest. The amount of such losses is not deductible by the distributing estate or trust (Code Sec. 4690)(12)).

The amount of an allowable passive activity loss is computed on Form 8582, Passive Activity Loss Limitations. The amount of an allowable credit is computed on Form 8582-CR, Passive Activity Credit Limitations. Form 8582 should be completed first so that the deductible amount of net loss from real estate can be determined on Schedule F of Form 1040, the amount of a loss reported on Schedule C or F of Form 1040 can be determined, and the amount of a loss from a partnership or other fiduciary can be determined on Schedule E.

65-DAY ELECTION: A trustee of a complex trust can make a yearly irrevocable election to treat a distribution, or any part of it, made within the first 65 days of the trust's tax year as having been distributed to the beneficiary on the last day of the trust's preceding tax year. This 65-day election is also available to decedents' estates. The election is made by checking the box at Item 6 under "Other Information" on the bottom of page 2 of Form 1040.

GLOSSARY

Administrator/Administratrix – the person appointed by a court to take charge of the estate of someone who died intestate (without a will). An administrator's duties are defined by state law and are substantially identical to those of an executor.

Adverse Party – someone who holds both a substantial interest in a trust as a beneficiary and a power over the trust, if the beneficiary's interest will be adversely affected by the exercise or non-exercise of the power.

Beneficiary – someone who is entitled to receive property held in the estate or trust. A beneficiary's interest in the estate or trust assets is called a *beneficial or equitable interest* or *a beneficial or equitable title.*

Bequest – a gift of property by will.

Contingent interest – a contingent interest conditions a beneficiary's right to trust property on the occurrence of some future event. If the event does not occur the beneficiary has no right to the property.

Corpus – is the property placed in a trust – its principal or capital, as distinguished from its income. Capital gains treated as income for tax purposes may be allocated to corpus in fiduciary accounting.

Decedent – a person who has died

Descendent – a person who is an offspring, however remote, of a certain ancestor.

Distributable Net Income (DNI) – the income distribution deduction allowable to estates and trusts for amounts paid, credited, or required to be distributed to beneficiaries is limited to DNI. This amount is computed on Schedule B.

Dower/Curtesy – the surviving spouse's (wife or husband) interest in the deceased spouse's estate who died without a will.

Executor/Executrix – the person in charge of the estate of a decedent who died testate (with a will). The role of the executor is defined by the decedent's will and limited by state law.

Fiduciary – a trustee of a trust; or an executor, executrix, administrator, administratix, personal representative or person responsible for the estate or trust.

Grantor – sometimes called the settler or trustor, is the person who creates a trust and/or transfers property to it.

Income in respect to a decedent (IRD) – income that was owed to the decedent but that was not received or accrued in income before death. Examples would be a final paycheck, individual retirement accounts, accrued interest on bonds, CD's, etc.

Inheritance Tax – a tax based on the right to receive property from a decedent's estate. The amount of tax is based on the beneficiary's share and relationship to the decedent.

Inter vivos trust – a trust that is created during the grantor's lifetime. It may be revocable or irrevocable. A revocable inter vivos trust is often called *a living trust.*

Intestate – when a person dies without a will or legal arrangements to dispose of property after death.

Irrevocable trust – a trust that cannot be altered or have assets withdrawn.

Revocable (living) trust – a trust that is created by a written agreement or declaration during the life of an individual and can be changed or ended at any time during the individual's life. This trust may be used instead of (or in addition to) a will.

Tax preference item – an item that can be legally omitted in order to reduce taxable income when calculating tax liability by ordinary means. However, the item must be included when calculating the alternative minimum tax. For example, interest paid by certain municipal bonds that is ordinarily omitted in calculating taxable income must be included when calculating the alternative minimum tax.

Testamentary trust – a trust created under a decedent's will. This trust by its nature is irrevocable.

Testate – when a person dies having made a legal will or arrangements to dispose of property after death.

Trustee – one who hold legal title to the trusts assets. The trustee may be an individual or a corporation/institution. The trustee is obligated to care for, manage, invest, and reinvest the trust property for the exclusive benefit of the beneficiaries.

Vested interest – a legal right to present or future enjoyment of property. The beneficiary can sell the interest unless it is otherwise restricted.

Will – a document prepared in contemplation of death and containing instructions for the disposition of property.

ADDITIONAL TYPES OF TRUSTS

Alaska Trust—This trust, available in certain states, combines the benefits of multigenerational planning (see Generation-Skipping Trust and Dynasty Trust) with an attempt at protection from the grantor's creditors. It has risks that must be carefully considered. Alaska trusts can last into perpetuity and pay no state taxes. They also are intended to compete with many of the "offshore" trust havens.

Blind Trust—This is a trust, often created by a politician after election to office, in which certain assets of the grantor are managed by one or more trustees without the grantor being advised of what assets are in the trust. The assets, however, are managed for the benefit of the grantor of the trust,

Cemetery Trust—This is a trust for the purpose of maintaining one or more graves or gravesites in a cemetery.

Charitable Lead Trust—This trust provides a specified sum to be paid to a charity at least annually, for a specified period, with the remainder passing to one or more individuals. The sum is expressed as a fixed percentage of the value of the trust at inception (in effect, an annuity) or a fixed percentage of the value of the net assets of die trust, calculated annually. If an annuity is utilized, it is a charitable lead annuity trust **(CLAT)**; if a percentage of the net assets valued annually is utilized, the trust is a charitable lead unitrust **(CLUT)**. Such trusts may save estate, gift, and income taxes.

Charitable Remainder Trust—This is a trust that provides one or more individuals, at least annually, either a sum equal to a fIxed percentage of the assets valued at the trust's inception (in effect, an annuity) or a sum equal to a fixed percentage of the net assets of the trust valued annually, either for a set number of years or for one or more lifetimes. If an annuity is utilized*,* the trust *is* a charitable remainder annuity trust **(CRAT)**; if a percentage of net assets valued annually is utilized, the trust is a charitable remainder unitrust **(CRUT)**. Such trusts may save estate, gift, income, and/or capital gains taxes.

Contingent Trust—This trust comes into being only in the event that a contingency occurs. For example, a document may provide that if any assets are distributable to a person under age 21 the assets are held in a contingent trust for the benefit of that person until he or she attains 21 years of age.

Crummey Trust—This trust permits one or more individuals to withdraw a limited amount from the assets added to the trust in a specified manner during a specified period. Its purpose is to avoid gift taxes on assets placed in the trust by qualifying the transfer for the annual exclusion. Insurance trusts (later in this list) are often designed as Crummey trusts.

Defective Grantor Trust—This is a type of trust purposely made "defective" so as to be a grantor trust for income tax purposes but an irrevocable trust (later in this list) for estate and gift tax purposes. It may result in increased tax savings.

Delaware Business Trust—Similar to a family limited partnership or limited liability company, as opposed to a traditional trust, a Delaware business trust is a way to hold and invest assets, possibly including life insurance, with greater flexibility than most trusts allow. The grantor of the trust retains far more control than the tax laws permit for traditional trusts. They can provide limited liability, creditor protection, and valuation discounts.

Disclaimer Trust—This trust is designed to receive property that is disclaimed (renounced) by a beneficiary. For example, it can be used to fund a credit shelter trust. It allows the *surviving spouse* to determine how much goes into the credit shelter trust after the death of the other spouse.

Discretionary Trust—This is any trust in which the trustees have discretion to distribute (or not distribute) income and/or principal among one or more beneficiaries. The discretion *may* apply to income, principal, or both. The trustees may have the right to give or not give income or principal to a single beneficiary, or to distribute some or all of the income or principal among members of a group, excluding one or more members of a group.

Dry Trust—This trust has no assets. A dry trust is usually created either to receive assets upon the death of an individual, such as a pour-over under the individual's will, or to receive assets transferred to the trust via a power of attorney in the event of an individual's incapacity.

Dynasty Trust—This is a name customarily used for a generation-skipping trust that continues for an extended period of time, such as for multiple generations, limited only by the applicable Rule Against Perpetuities, if any. In certain states such a trust may run for a very extended period of time. Its purpose is to avoid estate taxation for several generations and to provide for an individual's descendants (or the equivalent) for a very long period.

Educational Trust II.RC. § 2503(c) Trust— This is a trust for a minor (a person under the age of 18 or 21 years, depending on state law) designed to use the annual gift tax exclusion for gifts on behalf of the minor. I.R.C. § 2503(c) trusts are an alternative to the use of the Uniform Gifts (or Transfers) to Minors Act and are often a better way of planning with respect to gifts to children who are subject to the kiddie tax and whose parents are in a high-income tax bracket. An I.R.C. § 2503(c) trust can have provisions allowing more flexibility than is available under the Uniform Gifts (or Transfers) to Minors Act. Variations of this trust permit it to continue beyond the date on which the beneficiary attains the age of 21 years.

Estate Trust—This type of marital deduction trust (later in this list) provides that upon the death of the surviving spouse, the assets in the trust, or at least the accumulated income of the trust, are payable to his *or* her estate.

Foreign Situs Trust (Offshore Trust)—An individual who believes that assets cannot be fully secure while they remain under the jurisdiction of U.S. courts will seek havens outside U.S. boundaries where they can be safe from creditors (e.g., Switzerland, Liechtenstein, Isle of Man). This does not necessarily mean that assets can be hidden. There is in fact a high degree of economic intelligence data and disclosure to the IRS upon the formation or transfer to such offshore trusts. In the new global economic order, such trusts will continue to grow.

Generation-Skipping Trust—This trust either skips over an entire generation or provides for members of more than one generation, and is normally geared to utilize the exemption from the tax on generation-skipping transfers. Under federal law this exemption may be as much as $2,000,000 per grantor (not per trust and not per grandchild). The 45% (for 2007) generation-skipping tax applies to amounts in excess of $2,000,000.

Grantor Retained Annuity Trust (GRAT) This is an irrevocable trust created by an individual (the grantor) that provides the grantor, at least annually, a sum equal to a fixed percentage of the value of the assets placed in the trust (in effect, an annuity) for a fixed period of time or until the grantor's death. Upon termination, the balance in the trust usually passes to the grantor's estate if the grantor does not survive the term of the trust, or to other individuals if the grantor survives the term of the trust. Its purpose is to reduce gift and estate taxes. It serves little if any tax purpose if the grantor dies during the term of the trust. Note that it does not yield a step-up in basis of the assets in the trust if the trust terminates during the grantor's lifetime, and it is possible for the gift tax and resulting capital gains tax (assuming the assets are sold) to exceed the tax savings resulting from the creation of the trust. Note also that for income tax purposes it is a grantor trust (defined later).

Grantor Retained Income Trust (GRIT)— This trust, now only used in limited situations, is an irrevocable trust in which the grantor retains the right to income for a fixed period of years geared to end before the grantor's death. Upon termination of the trust, the assets in the trust pass to the final beneficiary. The main purpose of such a trust is to reduce the gift tax value of the transfer. The value of a promise to transfer an asset in the future is less than the current value of that asset. GRITs are now used for gifts to non immediate family members (e.g., nieces or nephews). Such a trust serves little or no tax purpose if the grantor dies before it terminates.

Grantor Retained Unitrust (GRUT)—This trust is very similar to a grantor retained annuity trust (see earlier definition), except that, rather than a fixed sum (a percentage of the assets of the trust valued at the creation of the trust), the grantor is to receive an annual (or more frequent) payment equal to a fixed percentage of the value of the net assets'of the trust valued annually during the term of the trust.

Grantor Trust—A grantor trust is any trust in which the grantor retains enough control to cause the income and capital gains to be taxed to the grantor even if not payable to him or her.

Insurance Trust—This is generally an irrevocable trust, designed to own insurance on the life or lives of one or more individuals and to provide for the disposition of the proceeds of such insurance. Unless irrevocable, an insurance trust serves no tax purpose whatsoever.

Inter Vivos Trust—This is any trust created during the lifetime of the person creating the trust. It is also called a living trust.

IRA QTIP—This is a type of QTIP trust specifically designed to receive the proceeds of an IRA. It requires specific provisions in the IRA and in the IRA QTIP Trust to qualify for the marital deduction and to avoid adverse income tax consequences.

Irrevocable Trust—This is any trust that may not be amended or revoked by the grantor. Transfers to such a trust may be subject to gift tax.

Marital Deduction Trust---This is any trust that qualifies for the estate tax (or gift tax) marital deduction. A marital deduction trust may provide, for example, that the spouse receive all of the net income for life, with the assets remaining in the trust passing to other individuals upon the spouse's death. It may also provide that the net income is payable to the spouse for life and give the spouse the right, either by will or by another specified instrument, to determine who receives the assets remaining in the trust upon that spouse's death.

Medicaid Trust-This is typically an inter vivos trust (defined earlier) for the benefit of the grantor or the grantor's spouse. Its purpose is to protect assets from creditors and to permit eligibility for Medicaid benefits. See also supplemental needs trust (later in this list).

Minority Trust—This is a trust geared to hold assets during an individual's minority or age specified in the trust.

Pour-Over Trust—This trust is funded from another instrument. For example, in a person's will the executor may be instructed to transfer (pour over) all or a portion of the assets of the estate to a trust created under another instrument.

Power-of-Appointment Trust—This is a trust over which an individual has a power of appointment; that is, the individual has the right to designate who will receive some or all of the assets of the trust at a specified time or times. A power of appointment may be exercisable either during life (an “inter vivos power”) or by will (a “testamentary power”).

Qualified Domestic Trust—This trust is very similar to a QTIF trust (defined earlier) but is meant for a surviving spouse who is not a citizen of the United States. A qualified domestic trust must have specific provisions regarding the distribution of income and principal, dealing with who may be trustees, and, unless an appropriate bank or trust company is a trustee, giving the I.R.S. a security interest with respect to future taxes. It is subject to special tax rules applicable only to such trusts.

Qualified Personal Residence Trust—This is a variation of a grantor retained annuity trust (defined earlier). It is a trust funded with the grantor’s residence or vacation home. It provides that the grantor may reside in the residence (or in another purchased with the proceeds of the sale of the residence) for a specified number of years, at the end of which the property passes to other persons. Its purpose is to reduce the value of the property for transfer tax *purposes.*

Rabbi Trust—This is not a typical trust arrangement but, in fact, a type of retirement plan or deferred compensation arrangement. The first one approved by the I.R.S. was created for a rabbi (thus its name).

Remainder man - the person who will receive a remainder in real property. One who receives the principal of a trust when it is dissolved.

Revocable Living Trust—This is a trust created during the grantor’s life that may be revoked by the grantor. It is used to avoid probate; to provide management during the grantor’s lifetime; to permit the administration, without additional (“ancillary”) probate proceeds, of assets (e.g., real estate) located in a jurisdiction other that the one on which the grantor resides; and sometimes for other purposes. Such trusts have the same income, gift, and estate tax consequences as wills and may or may not reduce administration expenses and legal and accounting fees. Revocable living trusts must be executed in accordance with applicable state law.

Second-to-Die Insurance Trust—This is a type of insurance trust (defined earlier) geared to one or more second-to-die insurance policies (also called survivorship or last-to-die trust).

Split Interest Trust - A Split Interest Trust is a trust that is treated like a charity although you still have a right to income from it for life. The trust is split into two interests, the present interest is treated as yours and the remainder is treated as charitable. A Split Interest or Charitable Remainder Trust can be used to avoid or reduce capital gains taxes, increase income, and avoid or reduce federal estate taxes. A Split Interest Trust can also be used as a retirement plan instead of an Individual Retirement Account. Unlike I.R.A.'s which can be exposed to liabilities, a Split Interest Trust is irrevocable and would not be subject to liabilities, thus assuring an income at retirement.

Spray/Sprinkling Trust—This is a discretionary trust for the benefit of a specified group, such as the grantor's spouse and descendants.

Supplemental Needs Trust—This is a trust for the benefit of an incapacitated person. It typically provides that its assets be available to be used for the benefit of that person, but the trustees are not to use trust assets to the extent that the incapacitated person would otherwise be receiving governmental benefits. Accordingly, it is possible, for example, for a parent to create a supplemental needs trust for an incapacitated child without interfering with the child's Medicaid benefits. Supplemental needs trusts often provide care *for* the beneficiary in addition to what Medicaid provides and deal with a beneficiary's nonessentials, such as paying for a vacation or a television. The use of supplemental needs trusts was expanded under provisions of the tax law enacted by Congress in 1993.

Unitrust – this type of trust, also known as a charitable remainder trust, is a legal device defined by federal tax laws that is frequently used by wealthy individuals who wish to make a substantial contribution to a school or charitable organization. To establish a unitrust, a donor transfers property to a trust, while retaining the right to receive payments from the trust for a term chosen by the donor. The payments may continue for the lifetime of the trust's named beneficiaries, a fixed term of not more than twenty years, or a combination of the two. Usually, the term is for the donor's life and the life of the donor's spouse. When the term has ended, the trust estate is paid to a public charity designated by the donor.

Wealth Replacement Trust—This is the name given to a type of insurance trust designed to hold insurance on the life of an individual, or an individual and spouse, and to use the proceeds of that insurance to replace assets passing to charity, such as upon the termination of a charitable remainder trust.

SUMMARY

This material in this manual should give you some basic insight about fiduciary income tax and serve as a reference guide for many issues concerning fiduciary tax. Fiduciary income tax, like other tax types, can be complex and require in-depth research for answers to issues.

KDOR employees should rely upon the following resources when seeking answers to fiduciary income tax questions and issues:

- Kentucky Revised Statutes & Administrative Regulations
  - ✓ 103 KAR 19:010
  - ✓ KRS 141.010
  - ✓ KRS 141.020
  - ✓ KRS 141.030
  - ✓ KRS 141.190
  - ✓ KRS 386.010
  - ✓ KRS 386.655
- All other Individual Income Tax Kentucky Statutes and Regulations
- Kentucky Form 741 and Schedules
- Kentucky Form 741 Instructions
- Federal Form 1041 and Schedules
- Federal Form 1041 Instructions
- 2008 U.S. Master Tax Guide – Chapter 5
- IRC
- CCH Publications

Website Assistance

Much more information is available and should be sought when needed. Many websites are available that address fiduciary income tax and provide useful information.

Some helpful sites for various tax issues and terms include:

- www.irs.gov
- www.reference.com
- www.taxsites.com
- www.taxprophet.com

For examples of various forms, such as trust documents, wills, bankruptcy declarations and other legal forms, these sites are available:

- www.allaboutforms.com
- www.lawca.com